Supreme Court, U.S.
FILED
APR 18 1990
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No. 89-1659

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1989

WILLIAM H. SCHNEIDER, et al.,
Petitioners,

vs.

APPLE COMPUTER, INC., et al.,
Respondents.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the Court of Appeals misconstrued *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988), by interpreting it to hold that, in a "fraud-on-the-market" securities fraud case, misrepresentations by company officials that otherwise violate Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder are "excused" as a matter of law if journalists and commentators opine that the company officials may be wrong?

2. Whether the materiality standard set out in this Court's opinion in *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976) applies to all Section 10(b) cases, or whether a different (and higher) standard of materiality applies in "fraud on the market" cases?

3. Whether, in a case under Section 10(b) of the Securities Exchange Act of 1934, this Court's summary judgment "trilogy," *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986), *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986), and *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986), empowers a trial court to take disputed factual issues such as materiality and scienter away from the jury despite the existence of conflicting evidence (including expert testimony) because the court simply rejects plaintiffs' evidence, finds it "dispelled" by contrary evidence or accepts defendants' proposed inferences from the evidence?

PARTIES

Plaintiffs and Appellants before the United States Court of Appeals were the Petitioners herein, William H. Schneider, Charles and Jeanne Cohn, Albert J. Whelan, Jr., and Estelle B. Ellis, on behalf of themselves and a class including all persons other than defendants who purchased Apple Computer, Inc. stock during the class period. Defendants and Appellees before the Ninth Circuit were the Respondents herein, Apple Computer, Inc. ("Apple") and several of its officers and directors: Gene P. Carter, John D. Couch, Wilfrid J. Houde, Steven P. Jobs, A.C. Markkula, Jr., Michael Muller, John Vennard, John Sculley, Delbert W. Yocam, and Kenneth R. Zerbe.[1]

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[1]The district court dismissed four "outside" directors of Apple, Defendants Peter O. Crisp, Arthur Rock, Philip S. Schlein and Henry E. Singleton from the action by order dated July 31, 1987, and because no appeal was taken as to dismissal of the four they were not parties to the proceedings before the Ninth Circuit.

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PETITION FOR WRIT OF CERTIORARI

The Petitioners William H. Schneider, Charles and Jeanne Cohn, Albert J. Whelan, Jr., and Estelle B. Ellis, on behalf of themselves and a class including all others similarly situated, respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit, entered in the above entitled proceeding and reported at 886 F.2d 1109.

OPINIONS BELOW

In the United States District Court for the Northern District of California, the Honorable Robert Aguilar, presiding: *In re Apple Computer Securities Litigation*, 672 F. Supp. 1552 (N.D. Cal. 1987) ("*Apple I*") [reprinted at Appendix B], *mod. on reh'g,* 696 F. Supp. 490 (N.D. Cal. 1987) ("*Apple II*") [reprinted at Appendix C], *and* 690 F. Supp. 872 (N.D. Cal. 1987) ("*Apple III*") [reprinted at Appendix D].

In the United States Court of Appeals for the Ninth Circuit, the Honorable Judges Farris, Boochever and Hall, presiding: *In re Apple Computer Securities Litigation*, 886 F.2d 1109 (9th Cir. 1989) [reprinted at Appendix A], *petition for rehearing and suggestion for rehearing en banc denied,* Jan. 18, 1990 [reprinted at Appendix E].

JURISDICTION

After the Ninth Circuit issued its decision, plaintiffs timely petitioned for rehearing and suggested rehearing *en banc*. The Court of Appeals denied rehearing and rehearing *en banc* on January 18, 1990, so that this petition for *certiorari* is timely filed by April 18, 1990. Jurisdiction is conferred upon this Court by 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS

Securities Exchange Act of 1934 Section 10(b), 15 U.S.C. § 78j(b):

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —
>
> * * *
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or

contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Securities Exchange Commission Rule 10b-5, 17 C.F.R. § 240.10b-5:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,
>
> (1) to employ any device, scheme, or artifice to defraud,
>
> (2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

STATEMENT OF THE CASE

A. Introduction And Overview

This case presents important questions regarding (a) the responsibility of corporate officers and directors to avoid insider trading and to be truthful in their public statements, and (b) the right to trial by jury, and the proper function of summary judgment, in a securities case alleging "fraud-on-the-market," a doctrine first approved by this Court in *Basic, Inc. v. Levinson,* 485 U.S. 224, 241-50 (1988).

Respondent Apple Computer, Inc. is a publicly-traded company which manufactures computers. Petitioners, a certified class of persons who purchased Apple stock during the Class Period (November 12, 1982 through September 23, 1983), alleged a fraudulent course of conduct by Apple and its top officers and directors, and sought relief under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder.[2] Plaintiffs alleged, and evidence was submitted supporting the allegations,[3] that Apple and its officers intentionally or recklessly misled the investing public regarding the business of Apple, and particularly regarding a new computer called "Lisa" and a disk drive called "Twiggy." Specifically, plaintiffs' evidence showed that, at a time when journalists and commentators were expressing uncertainty as to the prospects for Lisa and Twiggy, defendants made a series unqualifiedly positive representations about the capabilities and customer demand for Lisa and Twiggy to assure the investing public that Lisa would be successful. Evidence showed that the defendants knew but did not disclose:

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[2]The District Court had jurisdiction over this case pursuant to 15 U.S.C. § 78aa and 28 U.S.C. § 1331. The Court of Appeals had jurisdiction pursuant to 28 U.S.C. § 1291.

[3]For purposes of a summary judgment motion, the award of which is under review, "[t]he evidence of the non-movant is to be believed, and all justifiable inferences are to be drawn in his favor." *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 255 (1986).

a. that Twiggy and Lisa suffered severe technical deficiencies which would adversely affect Apple's marketing of Lisa;

b. that Apple's own pilot studies of Lisa users showed that customer reception would be unenthusiastic; and

c. that the much ballyhooed pre-introduction "backlog" of Lisa orders were cancellable at will and would evaporate as soon as users became aware of Lisa's limitations and deficiencies.

While carefully avoiding any disclosure of these facts, Apple proceeded with a continuous course of misrepresentations trumpeting Lisa and Twiggy's purported technical superiority, projecting "phenomenal" success for Lisa that would make Apple's previous (and prodigious) success "look small," and heavily publicizing the huge but misleading pre-introduction "backlog" of orders. Subsequently, as the truth about Lisa became known, the "backlog" of orders evaporated and the value of Apple stock plummeted by a total of nearly 75%, including a 25% (8 point) drop in one day on tremendous volume of twelve million shares, evidencing the public's surprise when Apple belately made negative revelations about Lisa. Lisa and Twiggy were total failures.

Moreover, while plaintiffs were purchasing Apple stock, Apple insiders sold over 1.5 million of their own shares during the Class Period — and another 847,553 shares in the 30 days immediately preceding it — for total proceeds of over $84 million. ER 11:876; ER 15:1043-47.

Plaintiffs intended to prove at trial that Apple's misleading statements inflated the market price of its stock, and that defendants knew their statements to be misleading — a classic case of "open market" Section 10(b) liability. *See generally Basic, Inc. v. Levinson,* 485 U.S. 224 (1988); *Blackie v. Barrack,* 524 F.2d 891 (9th Cir. 1975), *cert. denied,* 429 U.S. 816 (1976). But that trial never occurred. Instead, the district court fragmented plaintiffs' case into 16 separate "statements," and in three successive opinions granted summary judgment to defendants on all 16 on a variety of grounds. Among the bases for the district court's

judgment was that, at the time Apple was making these misrepresentations, some financial commentators expressed the opinion that Lisa might not succeed (without providing, or indeed knowing, most of the underlying details known to Apple). These conflicting opinions from outsiders were held to render Apple's misstatements immaterial *as a matter of law!* The Court of Appeals affirmed as to 14 of the 16 statements, expanding this unprecedented misinterpretation of Section 10(b) by finding that the misstatements were "excused" by the mixed opinions in the market, Appendix ["App."] at 10a, and asserting that this Court's intervening decision in *Basic* confirmed the availability of this novel defense. App. at 9a-10a. The court also announced a new double standard of materiality: the traditional standard for "ordinary" cases, and a higher standard for "fraud on the market" cases. App. at 8a. *No other case has ever so held.*

Leaving aside the question whether securities violations can be excused by virtue of third party commentary, *compare In re Western Union Securities Litigation,* 120 F.R.D. 629, 638 (D.N.J. 1988), under any reading of the law, the Court below misconstrued *Basic* by usurping the function of the jury. Thus, although the most favorable construction of *Basic* to the defense would require that the information withheld by Apple "credibly" enter the market from other sources and completely "dissipate" the effects of Apple's misstatements before the company's conduct could be said to be immaterial or harmless, 485 U.S. at 248-49 & n.29, the courts below took these heavily disputed and crucial *factual* issues away from the jury. Summary judgment was entered despite the fact that (a) the voluminous record, which fills an entire filing cabinet contains conflicting evidence on virtually every issue raised in the case; (b) plaintiffs offered expert testimony directly contrary to the court's central holding; and (c) the price movement of Apple stock, which lost nearly 75% of its value when the truth about Lisa was finally revealed by Apple — falling by 25% (8 points) on one day alone — demonstrated that the truth was *not* known to the market earlier.

The Court of Appeals committed these grievous errors by setting itself up as an expert upon finance, and then demonstrating that it was not with its misinterpretation of economic data.[4] *Compare Basic,* 485 U.S. 252-53 (White, J., dissenting in part) (condemning "economic theorization by the federal courts" which have "no staff economists, no experts schooled in the 'efficient-capital-market hypothesis' "). It compounded that error by rejecting the testimony of plaintiffs' expert, whose testimony has been accepted in several other cases, by holding that the financial economics issues presented "do[ ] not require any special competence." App. at 14a.

The Court of Appeals also held, as to the same 14 "statements", that summary judgment could be affirmed for lack of scienter, accepting defendants' claims of good faith, and rejecting all of plaintiffs' evidence — which included massive insider selling by the defendants — as not even raising a factual issue. App. at 14a-17a. As to 12 of the 14 statements, the Court of Appeals made *de novo* findings of no scienter where the district court had not even reached

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[4]The Court of Appeals stated that "it is a basis assumption of the securities laws that the partially informed investors will cancel each other out . . . . " App. at 9a. Nothing in the securities laws, any precedents, or the study of finance, indicates that conflicting misinformation automatically "cancels" itself. The precedents indicate the contrary — that "the market price of shares traded on well-developed markets reflects all publicly available information," *Basic,* 485 U.S. at 246, including misleadingly incomplete representations of corporate insiders. *See, e.g., In re Western Union Securities Litigation,* 120 F.R.D. 629, 638 (D.N.J. 1988). The Court also dismissed as irrelevant "[d]ramatic price movements" in response to Apple's public representations, including the precipitous drop in the value of the stock when the truth was revealed, on the ground that "the evidence of stock price movements provides no rational basis for determining whether Lisa's risks were adequately conveyed to the public." App. at 13a. Yet many cases have held such dramatic price drops on disclosure are evidence that the market previously was misled. *See, e.g., Kronfeld v. TransWorld Airlines, Inc.,* 832 F.2d 726, 735-36 (2d Cir. 1987), *cert. denied,* 485 U.S. 1007 (1988); *see also* 3 A. Bromberg & L. Lowenfels, *Securities Fraud & Commodities Fraud* § 7.4 (337) at 7:158.42 (1986).

the issue. *Compare Isquith v. Middle South Utilities, Inc.*, 847 F.2d 186, 210-11 (5th Cir.), *cert. denied*, ___U.S.___, 109 S. Ct. 310 (warning against such review of the record by a Court of Appeals).

These two holdings are not only erroneous, they are plainly inconsistent with one another. On the one hand, the court held that negative facts about Lisa and Twiggy were so widely reported that they were known to the market as a matter of law. App. at 12a-14a. On the other hand, the court's finding of no scienter suggests or assumes that these negatives were *not known to Apple's insiders,* who were representing the enormous capabilities and customer acceptance of Lisa. App. at 14a-15a.

The decision below, if left standing, will adversely affect most § 10(b) cases involving publicly traded companies, including SEC enforcement actions. Although the Court of Appeals suggested that the heavy press coverage of Apple was unusual, App. at 12a-13a, in fact most publicly traded companies are closely followed by the national financial press and by securities analysts. Thus this new defense will be presented in case after case, as corporate officials caught in lies will assert that their misstatements were rendered irrelevant because the market was apprised of the truth by "credible" commentators. It is important for this Court to determine (a) whether such a defense exists, and (b) if so, the proper role for the judge and the jury, respectively.

The decision below will also undermine the full disclosure objective of the federal securities laws, which are intended "to achieve a high standard of business ethics in the securities industry." *Basic,* 485 U.S. at 234; *see id.* at 230. As stated by the SEC and quoted with approval by this Court in *Basic*:

> "To the extent that investors cannot rely upon the accuracy and completeness of issuer statements, they will be less likely to invest, thereby reducing the liquid-

> ity of the securities markets to the detriment of investors and issuers alike."

485 U.S. at 235 n.12. The decision below is contrary to that philosophy of primary reliance upon the issuer and will undermine public confidence in the securities markets. Further, to the extent that the decision creates an unwarranted defense in investor class actions, which routinely employ the "fraud-on-the-market" doctrine, it will diminish the deterrent effect of such actions upon corporate fraud, which this Court has noted with approval. *See, e.g., Randall v. Loftsgaarden,* 478 U.S. 647, 664 (1986); *Bateman Eichler, Hill Richards, Inc. v. Berner,* 472 U.S. 299, 310, 315 (1985).

B. Apple's Course of Misrepresentation

1. The False and Misleading Statements

Record evidence showed that both before and throughout the Class Period defendants were repeatedly put on notice of very serious technical deficiencies in Lisa and Twiggy, and of severe shortcomings in Apple's plans to market Lisa. Although internal Apple memoranda indicated that the technical deficiencies would adversely affect Apple's efforts to market Lisa, and Apple's own consumer research indicated that customer reception would be poor, Apple nevertheless made a series of optimistic statements characterized by the Court of Appeals as "unqualified exuberance," App. at 12a, without disclosing the many crucial problems with Lisa and Twiggy.

Plaintiffs' allegations of a course of fraudulent misrepresentations began with Apple's November 12, 1982 Annual Report, which projected continuing "unequalled strength" and success in 1983 and beyond based on plans to introduce new products — of which Lisa and Twiggy were a crucial part.[5] This early announcement ignored already known negative information that had been generated from internal

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[5]The courts below broke these representations into statements they numbered "1," "2," and "3". They appear at App. F.

studies about poor customer reception,[6] deficiencies in Lisa's software,[7] and other technical problems with Lisa and its disk drive Twiggy.

On the very day of this bullish Annual Report, Apple's top executives and Board of Directors were warned:

> We are extremely concerned over the results of our latest run of Twiggy tests. As of 11/12, the current production units show a very high failure rate with an unknown mode. The current units will show a very high out of box failure rate and we suspect most of them will fail during the warranty period. This level of problems is frightening, considering we are building shipable Lisas beginning in December.
>
> * * *
>
> As of now, the Twiggy reliability would lead us to DELAY THE INTRODUCTION OF LISA BY MANY MONTHS. (Appellants' Excerpt of Record on Appeal ["ER"] 7:498.)

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[6]Early test marketing of Lisa demonstrated that potential customers were not enthusiastic about the machine. In April 1982, it was reported within Apple that, after tests with prospective purchasers, their "reactions to Lisa were overall, disappointing," "most respondents were skeptical about the system's value for them," and "were not strongly interested in the system, even after seeing it demonstrated." Appellant's Excerpt of Record before the Ninth Circuit ["ER"] 7:462, 468, 463. In May 1982, an Apple marketing consultant reported to defendants that, based on his study of potential Lisa customers, "interest in the Product appeared to be limited," and "it is our opinion that overall attitudes to the Product were disappointing . . . and not providing appreciable assurance about Lisa's commercial success." ER 7:474, 480. And in October 1982, another Apple consultant warned defendants that "Apple must control its ebullience about Lisa," and that "the market is extremely price sensitive and Apple is taking a distinct risk by betting that users will overlook Lisa's higher price and see its underlying value." ER 7:490, 491. None of this information was disclosed by Apple during the class period.

[7]Apple's management was aware that the third-party software so "vital" to Lisa's success was lacking. ER 7:484, 495.

On November 29, 1982, Apple issued a press release regarding Twiggy which contained misrepresentations subsequently numbered "4" and "5" by the courts below. App. F. (These are the two statements as to which summary judgment was reversed, App. at 10a-12a.)

Thereafter, conflicting information continued to enter the market regarding Lisa. Journalists expressed a wide array of opinions, but Apple continued outwardly to express supreme confidence despite internal documents reflecting serious problems. For example, although evidence reflected that Apple had little faith in Twiggy and Lisa,[8] on January 19, 1983, Apple issued a press release heralding the introduction of Lisa.[9] Then the January 31, 1983 *Business Week*

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[8]In December 1982, top executives were informed that Apple should be seeking help from an outside disk drive company, and that defendant Jobs had "virtually zero" confidence in the Twiggy division. ER 7:756. In January 1983, the top executives and Board were again warned:

> Our over-riding concern is still Twiggy.... If we do not start receiving at least 60 disks a day by midweek (Jan. 20) then the program is going to get into SERIOUS TROUBLE. (ER 7:787.)

A comprehensive internal analysis of Lisa in January 1983 concluded:

> We face a risk in introducing Lisa with almost no software other than what we are providing. We know that this was a significant problem in the Apple III introduction. (ER 7:508.)

However, such marketing risks were *never* disclosed to the investing public during the class period.

[9]These representations, numbered "6" by the district court and Ninth Circuit, were as follows:

> *Lisa incorporates the latest software and hardware technology....* Using LisaTerminal, a telecommunication software package being developed by Apple, Lisa functions as ... an IBM-compatible terminal. When linked to Apple-Net, Apple's newly announced local area network, Lisa makes it possible for users to share peripherals and exchange information and files.

App. F. The "latest software and hardware technology" incorporated in Lisa included Twiggy, which was actionably misrepresented in statements 4 and 5, even in the Ninth Circuit's eyes. App. at 10a-12a. The Court of Appeals never explained how statement 6 can be treated

carried a story which, while noting that outside analysts were uncertain about Lisa's prospects, published Apple's reassurances that it would be a tremendous success:

> Apple will not disclose its own internal sales forecast, although [Apple's Chairman Steven P.] Jobs says, "*I don't think we will have any trouble selling all the Lisas we can build.*"[10]

In fact, problems were so severe that in February 1983, defendant Jobs acknowledged in an internal memo, "our current decaying confidence in the Peripheral Division's ability to bring Twiggy to volume production". And Lisa's problems were not confined to Twiggy or to poor customer reception in Apple's studies. In March 1983 an internal report indicated that "there are several serious problems in regard to [Lisa's] out of box failures," ER 7:766, and Apple internally imposed an "immediate quarantine . . . on all Lisa finished goods." ER 7:577.[11]

Despite these problems, Apple proceeded to issue a string of additional glowing public representations about Lisa to an uncertain and information-hungry market. Projections of huge success for Lisa were presented in an April 14, 1983 *Wall Street Journal* article which quoted Apple officers to the effect that:

> "Lisa is going to be phenomenally successful in the first year out of the chute."

* * *

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differently, as *nonactionable*, although its misrepresentation mirrors and builds upon those of statements "4" and "5".

[10]App. F. (emphasis added). The courts below labeled Jobs' misrepresentation number "7." *Compare* Jobs' real views, described in note 8, *supra*.

[11]On April 4, 1983, top executives were told: "We can't determine the cause of ⅓ to ½ of all Twiggy failures. . . . Bottom line: *we don't have any data to suggest that Twiggy is a production quality product.*" ER 7:760 (emphasis in original).

> "This division [that developed Lisa] is going to make Apple's growth before this look small."
>
> * * *
>
> [T]he Company has increased by 50% its estimate of how many machines it should make by the end of the 1984 first half. . . . "What we're finding is the reception of Lisa has just been very strong. . . . We find people willing to put down $10,000 without blinking an eye. . . ." [M]ore companies are willing to commit themselves to larger orders than Apple had expected. "They're talking larger numbers for their first order, and a quicker reorder" . . . .[12]

Apple was obviously trying to bury any outsider doubts in an avalanche of bold, positive statements. This approach continued in an April 28, 1983 quarterly report which represented that Apple was "extremely pleased with the market acceptance and orders to date for our Lisa personal office system."[13] The barrage of misstatements continued through the spring and into summer,[14] despite Apple's awareness of continuing problems with Lisa.[15] On July 15,

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[12]App. F. These statements were numbered "8," "9" and "10" by the courts below.

[13]App. F. The courts below numbered this representation number "11."

[14]See Statements 12, 13, 14 and 15, App. F.

[15]A May 18, 1983 memo, identified at least 25 defects, observing that "software bugs are serious and likely to cause Apple to invest significant support time . . . undoubtedly, a certain amount of customer dissatisfaction is going to be generated because of these defects." ER 7:689. In mid-June, after Lisa supposedly had been "successfully introduced" an Apple executive informed defendant Couch:

> TWIGGYS . . . TWIGGYS . . . TWIGGYS . . . At the end of May we received 100 new Twiggys. They were put under the same tests as preceding groups. Unfortunately, they exhibit EXACTLY the same failure rate as the older drives. We are very concerned. We know that many problems have been fixed, but it seems that we have not

1983, Apple's chief financial officer warned the Board and the executive staff that Apple was "being too optimistic about current business trends" and that the "sales forecasting process is not working." ER 7:609. Consistent with this observation, the board and executive staff were notified in mid-July that revenues from the Lisa in June were below forecast by $7.7 million (more than 40%). ER 7:608.

Still, the positive public statements continued. In a July 27, 1983 Quarterly Report[16] Apple asserted that:

> Customer shipments of the Lisa system began on schedule and we remain pleased with its market acceptance, order rate and dealer enthusiasm. Lisa is clearly being recognized as an important force in the office market.

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yet solved the particular problems causing the drives to fail when run in LISA. (ER 7:743.)

The Lisa sales and backlog figures provided to defendants (but not to the public) demonstrate how poorly things were going. Between June 10, 1983 and June 27, 1983, Apple's internal estimate of the Lisa backlog decreased by 4,000 units, i.e., approximately 25%. *Compare* ER 7:623 *with* ER 7:586.

In July, in order to create paper sales of Lisa:

> Sales orders were processed for all of the Lisas allocated through the end of the year. This does not represent hard business. It was done at the strong insistence of sales [even though] . . . Lisa failures are running high and finished goods stock was pulled to provide spares when necessary. (ER 7:621-22.)

Of the companies to which Apple shipped Lisas for testing purposes, "45% had Lisas that broke during the study." ER 7:579. The final Lisa reliability report disclosed that 63.3% of the Lisa systems failed. ER 7:590. On July 12, 1983, the acting head of the Lisa division wrote to defendant Sculley and others and stated that "[t]he key problem [with Lisa] continues to be the out-of-box failure rate. . . . There is an ever growing sentiment that 'we have lost it in the large office.' " ER 7:633.

[16]App. F. Numbered "16" by the courts below.

On the contrary, Apple was actually aware that customers familiar with Lisa were not enthusiastic about the product,[17] and that inadequate software and other defects would cause serious dissatisfaction. These negatives were quickly borne out, and dealers cancelled shipments. ER 7:634. By August 15, the Lisa domestic order backlog fell from 11,000 [ER 7:586] to zero in just over one month.

By August it was clear internally at Apple that Lisa and Twiggy were a disaster. However, on August 15, Apple executives recommended that Apple continue its policy of concealment, instructing that there should be no public announcement that Twiggy — which had been cancelled *five months earlier* — would not be released, because "we do not want to stir up negative feelings which could seriously damage Lisa's image and sales." ER 17:1078. Dealers were instructed to lie if asked about Twiggy." *Id.*

In sum, the evidence showed a calculated course of misleading public representations intended to boost public (including investor) confidence in Apple and to alleviate uncertainties among outsiders as to whether Lisa and Twiggy would be successful.

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[17]A memo distributed to Apple executives in May or June 1983 evaluated customer reactions more honestly, reporting that "Apple continues to be met with a high level of incredulity at these accounts," and described "mixed impressions of Lisa from this group of initial Lisa users." ER 7:548, 545. Of the seventeen major corporations which were Lisa evaluation sites, fourteen were either critical of Lisa or had requirements which Lisa could not serve; nearly half were reported to have only a low to medium probability of actually purchasing Lisa. ER 7:551-68. And these were supposedly Lisa's "high potential" accounts! ER 7:545. A June 1983 internal report of interviews with these selected users concluded that many were reluctant to purchase Lisas because: "(1) The systems people lack confidence in Lisa's data communications capabilities. Lisa is considered a standalone, a stranger in an IBM environment; (2) The price is too high or not worth the functions Lisa offers — the problem of cost justification; (3) Lisa was looked at as a toy, not a business machine." (ER 7:529.)

Class members — purchasers during this period — paid stock prices which reflected Apple's fraudulent statements, even if somewhat tempered by the mixed views of journalists. Apple stock rose from $32 on November 12, 1982, to a high of more than $62 on June 6, 1983, just after statement 14, approximately the peak of Apple's "hype" of Lisa.

2. Apple Belatedly Discloses the Truth

From its peak on June 6 through mid-September, Apple's stock price steadily slipped, as the market began to comprehend that Lisa and Twiggy had serious problems. The market's reaction contradicts the Court of Appeals' finding that, as a matter of law, the market knew all it needed to know throughout the class period, even as the stock climbed in January, February, April and May, and peaked in June before tumbling catastrophically in September.

Indeed, on September 23, when Apple made the startling revelation[18] that its fourth quarter earnings would be "sharply lower" due, in part, to "flat sales" and "special writeoffs," related to Lisa and Twiggy, the already lower stock price evidenced the market's prior lack of full knowledge by dropping another 25% (8 points) in one day on 12 million shares traded — over 20% of Apple's outstanding stock changed hands. This huge price drop is utterly inconsistent with the Court of Appeals' central holdings that (a) the market indisputably knew what it needed to know throughout the class period, (b) Apple's dishonest statements indisputably had no impact on market price, and (c) honest disclosure by Apple indisputably would have been immaterial to the market. Thus the actual performance of the stock proves the Court of Appeals wrong — at a minimum it raised factual issues for the jury. But the jury never got to review the market evidence, because the Ninth Circuit usurped for itself the fact finding function.

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[18]The press reported that "the news startled many investors." ER 16:1052.

3. The Insider Trading

Apple's misstatements and omissions are only half the story here. The record also reflected that Apple insiders had sold huge quantities of their personal stock holdings as they became aware of Lisa's and Twiggy's problems and as they made a series of optimistic statements and projections. During the Class Period, the individual defendants sold $84 million worth of their Apple stock (more than 2.2 million shares) at inflated prices.[19] This is the classic pattern of securities abuse — positive public statements while the insiders unload their stock — which plaintiffs would have presented to the jury as further evidence of scienter. *See e.g., Lilly v. State Teachers Retirement System*, 608 F.2d 55, 56 (1979), *cert. denied*, 446 U.S. 939 (1980). Of course, defendants had their "explanations" for the sales. For example, one defendant asserted that he didn't sell his stock to avoid losing money in the coming downturn when Lisa's failure became public, but instead "needed" the money — to buy a house in Vail for $600,000 cash and a house at the beach for $250,000 cash! Whether to accept plaintiffs' inference or defendants' explanations is a classic jury question. Unfortunately, unless this Court acts, a jury will never hear this evidence because the district court and the Court of Appeals usurped the jury's function by accepting all of defendants' explanation.

C. The Opinions Below

Upon defendants' motions, and in three opinions, Judge Aguilar split plaintiffs' claim into sixteen separate claims, one for each "statement," and then proceeded to render summary judgment for defendants as to each. The district

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[19]Most individual defendants sold large portions of their Apple stock (*e.g.*, Yocam — 100%, Carter — 47%, Couch — 26%, Houde — 57%, Muller — 45%, Vennard — 60%, Zerbe — 28%). *See* ER 11:876; 15:1043-47. One defendant sold a huge amount of his stock just before the Class Period, when the situation was not materially different, as he was in a position to know Lisa and Twiggy were troubled products likely to fail.

court used a variety of labels to dispose of the entire case — materiality, scienter, "mere puffing," et cetera.

On appeal, the Ninth Circuit reviewed the matter *de novo*, implicitly rejecting many aspects of the district court's reasoning, but nevertheless affirming as to 14 of the 16 "statements." It affirmed on the 14 statements because (a) it found as a matter of undisputed fact that the market's awareness of certain commentators' doubts about Lisa *"excused"* any misstatement or omissions by defendants, App. at 10a; and (b) it found that plaintiffs' evidence of scienter — internal documents reflecting the contrary of what was said publicly, combined with insider trading — was insufficiently probative to get to the jury, or was "disspelled" by contrary evidence. App. at 14a-17a.

As noted above, these holdings are not only erroneous, taking two crucial disputed fact issues improperly from the jury, but they are internally inconsistent. *How can Apple's problems be so obvious and widely reported that they were conclusively known by "the market," but so non-obvious that they could be overlooked in good faith by Apple's top executives?* In fact, the Ninth Circuit got it precisely wrong — the problems were well known inside Apple, but were only partially understood by the public, making Apple's reassuring representations and omissions both highly material and intentionally misleading. At bottom, however, both of these issues were for the jury.

The Ninth Circuit's opinion reflects two fundamental misunderstandings of this Court's recent precedents. First, the Court purported to apply a passage from *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988), but badly misconstrued what this Court had to say, ignoring, *inter alia*, that whether a fact "credibly" enters the market and "dissipates" prior misstatements *is a question of fact for the jury! Basic*, 485 U.S. at 248-49 & n.29. The Seventh Circuit has taken a diametrically different approach to this issue, *Flamm v. Eberstadt*, 814 F.2d 1169 (7th Cir.), *cert. denied*, 484 U.S. 853 (1987), and the First Circuit has the issue under

consideration *en banc. Backman v. Polaroid Corp.*, 893 F.2d 1405 (1st Cir. 1990), *reh'g en banc granted,* (Feb. 28, 1990). Second, the Court of Appeals misapplied this Court's summary judgment "trilogy," reading into those cases broad license to weigh evidence, reject expert testimony, and draw inferences against the party opposing summary judgment.

It is these fundamental errors in applying *Basic* and the summary judgment trilogy, or in reading those two lines of authority together, which require this Court's review. Given the importance of the fraud on the market theory recently approved in *Basic*, and the important role of private class actions in enforcement of the securities laws, including insider trading restrictions, the decision below cannot be allowed to stand.

ARGUMENT

The Ninth Circuit misconstrued securities and summary judgment law in several important respects. First, it held that where misleading statements are made to reassure an uncertain market, the very uncertainty of the market, which in part motivated the fraud, also "excuses" the fraud. The Court of Appeals erroneously found this new defense to securities liability in this Court's holding in *Basic,* which, as illustrated below, would have come out contrary to the holding of this Court under the Ninth Circuit's analysis.

Second, the court announced that there are two materiality standards, one for "ordinary" cases, and the other for "fraud on the market" cases. App. at 8a. This holding is unprecedented and erroneous, as materiality is an objective standard.

Third, the Court of Appeals erroneously rejected plaintiffs' evidence, weighed evidence, and drew inferences against plaintiffs, on defendants' motion for summary judgment, believing it was permitted to do so by this Court's summary judgment "trilogy." The trilogy contains no such license to resolve genuinely disputed issues.

Each of these holdings will be followed in the Ninth Circuit, and potentially elsewhere, and will do serious damage to enforcement of the securities laws. *Certiorari* is necessary so that this Court may review and correct the Ninth Circuit's serious legal errors, and further explicate its holdings in *Basic* and the summary judgment trilogy.

A. *Certiorari* Should Be Granted Because The Ninth Circuit Misconstrued *Basic* And Is In Conflict With The Seventh Circuit In Holding (1) That The Existence Of Conflicting Opinions Of Journalists And Others As A Matter Of Law "Excuses" Fraudulent Misrepresentations, and (2) That There is A Different Standard of Materiality in Fraud on the Market Cases

The most egregious error committed by the Ninth Circuit, and one that will create the most serious problems and confusion if not promptly corrected by this Court, is its holding that otherwise actionable fraudulent misrepresentations by company officials are "excused" as a matter of law if they are made into a market which is hearing contrary statements from outsiders. App at 10a. In other words, the court held that, where there is a wide array of outsider opinion on how a company will fare, its top officers are *free to lie* in public statements, because the "truth" is out there in the market — somewhere! This holding is without precedent, is contrary to the law established in over 50 years of litigation under the 1933 and 1934 Securities acts, and although purportedly drawn from *Basic*, in fact conflicts irreconcilably with that decision.

The evidence which plaintiffs intended to present to the jury tended to show that defendants intentionally made untrue or misleading optimistic representations and projections regarding Lisa, notwithstanding their knowledge of severe problems, in part so that they could sell millions of shares of their Apple stock at inflated prices before the bad news was fully revealed. The Ninth Circuit acknowledged that "many of these statements failed to disclose material risks," App. at 12a, and assumed that the misleading state-

ments *in fact* had an impact on Apple's stock price,[20] but nevertheless exonerated the defendants because *"it is a basic assumption of the securities laws that the partially-informed investors will cancel each other out, and that Apple's stock price will accurately reflect all relevant information."* App. at 9a (emphasis added). Just where this assumption is taken from is unclear. Not from the language of the statute, nor the legislative history. The Ninth Circuit cites no authority other than this Court's opinion in *Basic*. *See id.*

Basic, of course, contains no such holding, nor does any finance or economics treatise. On the contrary, "if relevant information is withheld from the market, or if incorrect information is disseminated, the price of stock will be mispriced, causing some investors to be injured." Fischel, *Use of Modern Finance Theory in Securities Fraud Cases Involving Actively Traded Securities,* 38 Bus. Law. 1, 5 (1982). Indeed, this Court recognized in *Basic* that empirical studies confirm "that the market price of shares traded on well-developed markets reflects *all publicly available information, and, hence, any material misrepresentations.*"[21] In *Basic,* this Court accordingly held that materiality of misrepresentations, and their impact on the market — including the extent to which information already in the market may minimize that impact — are *issues of fact for the jury. Basic,* 485 U.S. at 249 n.29. The Ninth Circuit purported to follow *Basic,* but completely missed this Court's reasoning and holding.

The Ninth Circuit recognized that statements like those in this case would be actionable in an individual securities fraud case, App. at 8a, but held that they were immaterial as

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[20]App. at 13a (assuming that dramatic stock price changes reflected the fact "that the market was persuaded by Apple's optimism").

[21]485 U.S. at 246 (emphasis added) (*citing In re LTV Securities Litigation,* 88 F.R.D. 134, 144 (N.D. Tex. 1980) (citing studies); *Fischel, supra* at 4 n.9 (citing literature on efficient-capital-market theory); Dennis, *Materiality and the Efficient Capital Market Model: A Recipe for the Total Mix,* 25 Wm. & Mary L. Rev. 373, 374-81 & n.1 (1984)).

a matter of law when a class of innocent investors sues under the fraud-on-the-market doctrine. *Id.* Leaving aside the double standard of materiality, *see infra,* the emphasis in the decision below on the fact that "many of the risks" were publicized, App. at 4a, grossly oversimplifies the situation, assuming that mere disclosure that there is a "risk" will satisfy the securities laws, and ignoring the myriad distinctions in the eyes of the securities market between full disclosure by insiders and mere speculation by commentators whose opinions are "all over the ballpark."

Indeed, for these very reasons, the decision below is in direct conflict with Judge Easterbrook's well-reasoned decision for the Seventh Circuit in *Flamm v. Eberstadt,* 814 F.2d 1169. Addressing this very question, the court held that *"[k]nowledge of a risk does not prevent recovery if the additional information [withheld] would have been a significant increment to the total available knowledge." Id.* at 1173 (emphasis added). Even with the doubts expressed by outsiders, Apple's own concerns about Lisa, and the detailed underlying information which caused those concerns, would have been a "significant increment to the total available knowledge" in the market, *Flamm,* 814 F.2d at 1173. At a minimum, a jury question was presented.

The holding below also conflicts with *TSC Industries, Inc. v. Northway, Inc.,* 426 U.S. 438, 449 (1976), which announced an objective standard for materiality, and *Basic,* which applied that standard to a Section 10(b) fraud on the market case. If the standard is objective, how can it vary between a face-to-face fraud and a fraud on the market? The Ninth Circuit's double standard of materiality, App. at 8a, is entirely novel, and equally erroneous.

Moreover, the Ninth Circuit was obliged to invent this double standard because its materiality holding cannot be reconciled with *Northway,* which holds that materiality must be judged based upon the "total mix of information" in the marketplace. Even if the market knew that Lisa posed some undefined "risk" to Apple, the "total mix" of information in the marketplace would surely have been changed by Apple's

ebullient, unqualified, and seemingly authoritative statements. Thus the court below ignored the impact of Apple's misstatements and omissions upon the "total mix," purporting to answer that inquiry simply by finding that there *was* a mix.[22]

As noted above, the decision below, although purportedly based upon *Basic,* is so irreconcilably inconsistent with *Basic,* that the *Basic* case itself would have come out the other way under the principles applied here. In *Basic,* the defendants were charged with issuing misleading statements in connection with possible merger negotiations. In *Basic* the truth — that there were negotiations — *had begun to enter the market in the form of Wall Street rumors.* Defendants issued statements denying the rumors:

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[22]The holding also conflicts with lower court holdings such as *In re Western Union Securities Litigation,* 120 F.R.D. 629, 638 (D.N.J. 1988), which flatly rejected the assertion that third party disclosures can excuse securities violations, noting that such a doctrine "would send [the wrong] message to corporations." The Court wrote:

> The moving parties also argue that the true state of the company and the markets in which it interacted was being reported by the national media. As a result, we are told, accurate information existed in the marketplace about Western Union, and the plaintiffs were exposed to this information in the media.
>
> We find this argument incredible, especially since it almost appears to concede that Western Union's annual report and prospectus were misleading. Putting this curious aspect aside, we nevertheless find the argument without merit. Even if some curative information were available to the public, that would not eliminate the alleged misrepresentations that had also been disseminated. *That inaccurate information could certainly have played a role in setting an artificial market price.* . . . [A]cceptance of defendants' argument would send a message to corporations and others that they need not be bound by the disclosure requirements of the federal securities laws as long as they disseminate *some* accurate information to the market, or perhaps even if such information otherwise exists. Such a position would controvert the purposes behind rule 10b-5, and we refuse to adopt such a stance here.

120 F.R.D. at 638 (emphasis added in part).

> On October 21, 1977, after heavy trading and a new high in *Basic* stock, the following news item appeared in the Cleveland Plain Dealer:
>
> [*Basic*] President Max Muller said the company knew no reason for the stock's activity and that no negotiations were under way with any company for a merger. He said Flintkote recently *denied Wall Street rumors* that it would make a tender offer . . . .

485 U.S. at 227 n.4 (emphasis added); *see Levinson v. Basic, Inc.*, 786 F.2d 741, 744 (6th Cir. 1986).

> On July 14, the price of Basic's stock rose sharply . . . . Again Basic, through Thomas, denied that any undisclosed merger or acquisition plans or any other significant corporate developments existed. . . .
>
> On September 25, the price of Basic stock again rose. . . .

Basic, 786 F.2d at 745; *see* 485 U.S. at 227-28 n.4.

Merger negotiations continued, but *Basic* continued to deny the rumors. Subsequently the full truth came out when the tender offer was announced, and certain selling shareholders filed suit, claiming that they had been misled by the company's denials. This Court noted that:

> [T]here may be a certain incongruity between the assumption that Basic shares are traded on a well-developed, efficient, and information-hungry market, and the allegation that such a market could remain misinformed, and its valuation of Basic shares depressed, for 14 months, on the basis of the three public statements.

Basic, 485 U.S. at 249 n.29. But the Court instructed that *when and how the truth came out "is a matter for trial." Id.*

Of course, under the analysis of the Ninth Circuit here, the *Basic* shareholders would have no claim because the information they claimed had been omitted — the existence of merger negotiations — was the subject of many Wall Street rumors, strong enough to move the stock price. Thus,

the facts in *Apple* and *Basic* are indistinguishable on this point. However, *Basic* was remanded *for trial.*

The decision below is also counter to the basic finance and economic principles which it purports to follow. No rational economist would suggest that the market price of Apple stock would be the same whether Apple had disclosed its negative inside information or not. *Indeed, plaintiffs' expert opined directly to the contrary, and defendants tellingly failed to offer any expert on the subject.* (ER 13:941, 947.) The Court should have focused upon the issue identified by the Seventh Circuit in *Flamm* — whether "the additional information [withheld] would have been a significant increment to the total available knowledge." 814 F.2d at 1173. Applying *Flamm*'s test to the omitted information, (Apple's own view of Lisa, and underlying technical problems and marketing failures) might support summary judgment for plaintiffs, but at a minimum presents a jury question. But the Ninth Circuit never made any such analysis, instead holding that general expressions of uncertainty or "risk" in the market were enough disclosure.

In determining as a matter of law that journalists' opinions cured Apple's misstatements, the Court of Appeals leaped over several subsidiary issues. To meet the standard of *Basic*, the court would have to have found (a) that *all* of the arguably material omitted information entered the market through journalists, a palpably false assertion here given the crucial underlying details known only at Apple; (b) that the views of journalists were accepted by the market as "*credible*," rather than merely the views of a few skeptics, an issue ignored below;[23] and (c) that the information coming to the market from journalists totally "dissipated" and discredited Apple's misstatements and omissions, another

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[23] Had the Court looked at the issue, the evidence of record was plaintiffs' expert's declaration, which stated that outsider opinions are not credited to the same degree as issuer statements, and the stock price decline when Apple belatedly disclosed the truth, which points in the same direction. Defendants offered nothing on this issue.

factual issue ignored below.[24] Thus the court truncated the analysis under *Basic*, and thereby accepted Apple's defense as a matter of law, although Apple had not satisfied the elements identified in *Basic*.

Had the Court of Appeals properly applied *Basic*, defendants could not have made the required showing to prevail as a matter of law. Indeed, if the information was fully absorbed by the market, why, when Apple finally disclosed the truth, did "the news *startle[ ] many investors*" (ER 16:1052, emphasis added), causing a huge 25% price decline on massive volume in one day? Obviously, full disclosure by Apple had far greater impact than speculation by the press! Plaintiffs' expert opined that this huge market loss indicated that the market had been misled earlier and that the stock price had been inflated. ER 13:941-47.

The Court of Appeals excused Mr. Jobs' statements that "I don't think we will have any problem selling all the Lisas we can build"; and "Lisa is going to be phenomenally successful in the first year out of the chute," because the same *Business Week* article which quotes Jobs also states: "One indication of how uncertain Apple's prospects are is that expert estimates of how many Lisas the company will sell are all over the lot — from 2,000 to 30,000." App. at 4a. Can the Court of Appeal conceivably be correct that Mr. Jobs is free to make such a misleading statement, knowing that Lisa is encountering serious technical and marketing difficulties, and that his lie is excused merely because a wide array of opinions on Lisa are held by outside analysts? Is his purportedly authoritative lie indisputably immaterial to the market? These holdings turn securities law on its head.[25]

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[24] Again, had the court looked at the issue, the evidence was uniformly against defendants' position. *See* note 23, *supra*.

[25] Moreover, the statements by Apple exacerbated the situation because, given Apple's perceived superior knowledge about its own products, and its favorable track record, the statements tended to discount the unfavorable opinions in the market and confirm the favorable. Once again, plaintiffs' expert witness so testified (ER 13:947), but because

The Ninth Circuit's rationale is undermined by the efficient capital markets principles it purports to apply. If the market has a wide array of opinions on Lisa's prospects, and no useful information from management, Apple's stock might sell, hypothetically, for $45 per share. If Apple then announced that Lisa was a technological breakthrough, and selling well, the price might increase to $60, even though doubtful commentators persisted. However, the Court of Appeals would find that statement *per se* immaterial. If Apple subsequently announced that Lisa did not work and would not sell, the price might drop to $30. Again, any intentional delay in such an announcement would be, according to the Ninth Circuit, *per se* immaterial. The decision below would hold that persons who purchased at $60 would have no claim, even if they proved that Apple's positive statements were intentionally false. The opinion would hold that, because the market had a wide array of opinions, Apple was *immunized* from securities liability during this period.

Of course, defendants might have avoided securities liability by remaining mute about Lisa and not trading in Apple stock. But they did not do so. The law is clear that "a duty to speak the full truth arises when a defendant undertakes to say anything."[26] It is also axiomatic that one in possession of material information must disclose it or refrain from trading. *Chiarella v. United States*, 445 U.S. 222, 226-29 (1980). Defendants violated both principles by making misleading statements and by unloading large portions of their personal stock holdings without disclosing the adverse facts they knew about Lisa. Under any rational reading of Section 10(b), this case should have gotten to the jury.

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the court misconstrued *Basic* and believed itself expert in finance, it ignored the issue and rejected the expert testimony. App. at 13a-14a.

[26] *First Virginia Bankshares v. Benson*, 559 F.2d 1307, 1317 (5th Cir. 1977), *cert. denied*, 435 U.S. 952 (1978); *accord Roeder v. Alpha Industries, Inc.*, 814 F.2d 22, 26 (1st Cir. 1987); *Dominick v. Dixie Nat. Life Ins. Co.*, 809 F.2d 1559, 1571 (11th Cir. 1987).

The Ninth Circuit misinterpreted *Basic* in a way that conflicts with and vitiates the fundamental tenet of the securities laws "should be construed 'not technically and restrictively, but flexibly to effectuate [their] remedial purposes.' " *Herman & MacLean v. Huddleston*, 459 U.S. 375, 386-87 (1983). For this reason this Court has rejected narrow readings of § 10(b) in whatever guise they may be advanced. For example, this Court has "eschewed rigid common-law barriers in construing the securities laws," *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 310 (1985), rejecting the defenses of *in pari delicto* and unclean hands. *Id.* at 315-19; *see also Herman & MacLean*, 459 U.S. at 387-89; *Randall v. Loftsgaarden*, 478 U.S. 647, 664 (1986). Similar considerations motivated this Court's adoption of the presumption of reliance on material omissions in *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 151-54 (1972), and the presumption of reliance on the integrity of the market engendered by the fraud on the market theory. *Basic*, 485 U.S. at 242. The Ninth Circuit's holding that securities violations can be excused by heavy press coverage will seriously impair enforcement of the securities laws.

The Ninth Circuit badly misinterpreted *Basic* regarding the respective role of the market and the securities issuer, and only by doing so did it put itself into a position to find, as a matter of law, that Apple's misstatements and omissions were immaterial.

B. *Certiorari* Should Be Granted Because The Ninth Circuit Misconstrued This Court's Summary Judgment "Trilogy" As Allowing It To Invade The Province Of The Jury, Weigh Evidence, And Reject Expert Testimony

Before this Court issued its so-called summary judgment "trilogy," *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986), *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986), and *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986), it is unlikely that any court would have seri-

ously contemplated summary judgment in this case. On the two crucial issues, materiality and scienter, the voluminous record was loaded with conflicting evidence, and the parties were urging conflicting inferences from the evidence. For example:

— Plaintiffs urged that defendants' bold statements and crucial omissions were material to the investing public, relying upon expert testimony, stock price movement and common sense, while defendants urged that the market had sufficient information so that defendants' misstatements were immaterial;

— Plaintiffs urged that defendants' statements were made in bad faith or recklessly, based upon internal documents showing problems with those products, while Apple urged that the statements were good faith but erroneous projections;

— Plaintiffs urged that the insider trading evidenced bad faith and a knowledge that Lisa would fail; defendants urged that the sales were coincidental and made for other reasons.

Given the numerous authorities holding that both materiality and scienter are ordinarily questions for the jury unlikely to be disposed of on summary judgment,[27] and given the record here, plaintiffs submit that, prior to the trilogy, the notion of summary judgment on all (or the bulk)

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[27]The issues of materiality and scienter are intensely factual inquiries, suitable for determination at trial rather than on a preliminary motion. *See Basic*, 485 U.S. at 239, 248-49 & n.29. Materiality is a jury question which requires "delicate assessments" of what a reasonable shareholder would find significant, *Basic*, 485 U.S. at 236, and whether the market has absorbed information or remains misinformed "is a matter for trial," *id.* at 249 & n.29. Scienter similarily requires factual determinations which are particularly inappropriate for disposition on motion for summary judgment. *See, e.g., Herman v. Provident Mutual Life Ins. Co.*, 886 F.2d 529, 536 (2d Cir. 1989); *Ness v. Marshall*, 660 F.2d 517, 519 (3d Cir. 1981); *Smith v. Hudson*, 600 F.2d 60, 66 (6th Cir.), *cert. dismissed*, 444 U.S. 986 (1979).

of plaintiffs' claim would have been preposterous. The issue presented here is whether the trilogy changes that analysis by allowing trial courts to resolve disputed issues of fact, or whether, as *Celotex* says, the basic principles under Rule 56 have not changed. 477 U.S. at 325.

From the time the trilogy came down, lower courts, commentators and attorneys have been discussing whether those opinions changed the standards for summary judgment.[28] Indeed, the only explanation for the Ninth Circuit's decision here is that the Court of Appeals believes that there is a new standard for summary judgment, and the decision contains such language. For example, the Court says that summary judgment is not blocked by "any disagreement about a material issue of fact." App. at 5a. This Court's authorities are to the contrary. *See Anderson*, 477 U.S. at 247-48; *Matsushita*, 475 U.S. at 585-86. And the Court of Appeals says, purporting to follow *Anderson*, that summary judgment may be granted if plaintiffs' evidence is "not sufficiently probative," App. at 6a, ignoring the fact that *Anderson* was discussing whether evidence could meet the "clear and convincing evidence" standard, which is not implicated here. *See* 477 U.S. at 252-56.

That the Court of Appeals resolved numerous disputed factual issues is plain.

1. The Court decided that, because "the press portrayed Lisa as a gamble," App. at 12a, "the market could not have been made more aware of Lisa's risks," *id.*, thus finding

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[28] *See e.g.*, Friedenthal, *Cases on Summary Judgment: Has There Been a Material Change in Standards*, 63 Notre Dame L.Rev. 770, 771 (1988) (trilogy "appears to signal somewhat of a turn toward greater approval of summary dispositions"); Kennedy, *Federal Summary Judgment; Reconciling Celotex v. Catrett with Adickes v. Kress and the Evidentiary Problems Under Rule 56*, 6 Review of Litigation 227, 228, 230 (1987) (trilogy "generally favor[s] summary judgment for defendants" and "signal[s] a significant change in attitude toward grants of summary judgment"); *Street v. J.C. Bradford & Co.*, 886 F.2d 1472, 1476 (6th Cir. 1989) (noting that a "new era in summary judgments dawned by virtue of" the trilogy).

Apple's misstatements and omissions immaterial. Plaintiffs' evidence was to the contrary.

2. The Court found that the information omitted by Apple was "transmitted to the public with a degree of intensity and credibility sufficient to effectively counterbalance any misleading impression." *Id.* Plaintiffs' evidence was to the contrary.

3. The Court rejected plaintiffs' inferences based upon the rapid drop in Apple stock price after disclosure of the previously withheld material, instead adopting its own interpretation of the price movement, which it characterized as "plausible." App. at 13a.

4. The Court rejected the testimony of plaintiffs' finance expert to the effect that company statements are more heavily weighted by the market than outsiders' opinions, acknowledging that it was "problematic" to summary judgment, but nevertheless concluding that the record was "clear" and that it "does not require any special competence" to resolve this finance issue. App. at 13a-14a.

5. As to scienter, the Court chose to credit defendants' self-serving declarations of good faith[29] and a handful of internal positive indications about Lisa, rejecting plaintiffs' evidence from the files of Apple as showing "only . . . that Lisa's prospects were *uncertain*." App. at 15a. Leaving aside the fact that some of the evidence showed far more than mere uncertainty, where in the securities laws is it written that an Apple top official can represent that "Lisa is going to be *phenomenally successful the first year out of the chute*," (App. F, Statement 8) when he knew that success was "*uncertain*"? If there was to be a summary judgment on this issue, it should have been for plaintiffs.

6. With regard to insider trading, which plaintiffs also relied upon to show scienter, rather than accepting plain-

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[29]The Ninth Circuit thus disregarded this Court's warning in *Anderson* that its holding "by no means authorizes trial by affidavits" on defendants' motion for summary judgment. 477 U.S. at 225.

tiffs' inference that huge stock sales implied knowledge of the upcoming problems, the Court accepted defendants' assertions that the sales were for "innocent" reasons, such as defendant Couch needing the money to buy a house in Vail for $600,000 cash and another at the beach for $250,000 cash. *Compare Dolgow v. Anderson*, 438 F.2d 825, 828 (2d Cir. 1970) (reversing summary judgment because of such evidence). The court below also accepted defendants' interpretation of the sales pattern — that the large sales by one defendant just before the class period somehow rebutted the inference from all the other sales. App. at 15a-16a. Finally, the Court found that the inference sought by plaintiffs was "dispelled" by other evidence, including the fact that insiders' sold *only $84 million* worth of stock, retaining the majority of their vast holdings. *Id.* at 16a-17a. Unless the trilogy has changed the law, the inference to be drawn from these insider sales was plainly a jury question.

Contrary to the apparent views of the courts below, nothing in the trilogy changed basic summary judgment principles. *Celotox*, 477 U.S. at 324-25. "Credibility determinations, the weighing of the evidence, and the drawing of legitimate inferences from the facts are jury functions, not those of a judge, whether he is ruling on a motion for summary judgment or for a directed verdict. The evidence of the non-movant is to be believed, and all justifiable inferences are to be drawn in his favor." *Anderson*, 477 U.S. at 255; *accord Matsushita*, 475 U.S. at 587; "[T]he judge must ask himself not whether he thinks the evidence unmistakably favors one side or the other but whether a fair-minded jury could return a verdict for plaintiff on the evidence presented." *Anderson*, 477 U.S. at 252.

The trilogy dealt with procedural issues not presented here. *Celotex* addressed the movant's burden of going forward, not at issue here. *See* 477 U.S. at 323-24. *Anderson* addressed the effect on summary judgment of an ultimate standard of proof of "clear and convincing" evidence, not applicable here. 477 U.S. at 244. *Matsushita* addressed the

impropriety of drawing fundamentally implausible inferences of antitrust conspiracy from particular types of business conduct which this Court suggested should be encouraged as pro-competitive — again, not at issue here. *See* 475 U.S. at 593-98.

Thus the trilogy does not support the result below unless one reads it as sending a message to take factual issues from the jury when the Court believes it knows the "proper" result — even if contrary evidence and expert opinion is offered. Indeed, assertions that summary judgment standards have been radically altered by the trilogy are belied by *Basic,* in which the Court affirmed the *reversal* of a summary judgment on materiality issues in a Section 10(b) case, and remanded for trial, without once citing *Celotex, Anderson* or *Matsushita.*

In sum, the Ninth Circuit rode roughshod over the jury's fact finding function. Whether this stemmed from its misconstruction of *Basic* or from a misapprehension of the trilogy, it is grave error which must be corrected by this Court.[30]

DATE: April 18, 1990

LEONARD B. SIMON
Counsel of Record for Petitioners

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[30]The courts below also erred in reviewing this case under Rule 56 as if it were 16 separate claims, each founded upon a single misrepresentation, rather than a single lawsuit based on a unified and continuous course of misleading conduct. The lower courts' dissection of plaintiffs' claim is contrary to the law applied in the other circuits, *see, e.g., Isquith v. Middle South Utilities, Inc.*, 847 F.2d 186, 200-03 & n.9 (5th Cir. 1988), and is contrary to this Court's precedents. *See Continental Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 698-99 (1962).

APPENDIX

A

[886 F.2d 1109]

In re APPLE COMPUTER SECURITIES LITIGATION.

WILLIAM H. SCHNEIDER; CHARLES COHN; JEANNE COHN; ALBERT J. WHELEN, JR.; AND ESTELLE B. ELLIS; INDIVIDUALS, ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED, *Plaintiffs-Appellants.*

VS.

JOHN VENNARD; DELBERT W. YOCAM; MICHAEL MULLER; WILFRID J. HOUDE; JOHN D. COUCH; GENE P. CARTER; KENNETH R. ZERBE; STEVEN P. JOBS; A.C. MARKKULA, JR.; JOHN SCULLEY; INDIVIDUALS; AND APPLE COMPUTER INCORPORATED, A CALIFORNIA CORPORATION, *Defendants-Appellees.*

No. 88-1617.

United States Court of Appeals, Ninth Circuit.

Argued and Submitted Jan. 13, 1989.

Decided Sept. 25, 1989.

Before FARRIS, BOOCHEVER and HALL, Circuit Judges.

FARRIS, Circuit Judge:

This is an appeal from three orders which together granted summary judgment against plaintiffs on all of their claims under the Securities Exchange Act of 1934, 15 U.S.C. § 78a et seq. Plaintiffs allege that Apple Computer Inc. and its top officers misled the market about the capabilities and prospects of a novel office computer and disk-drive system. They claim that they purchased Apple stock in reliance on the artificially high stock price resulting from Apple's misrepresentations, and that they suffered actionable damages when the true facts about the computer became known and Apple's stock price fell by almost 75%. The trial court granted summary judgment on the grounds that each of Apple's alleged misstatements was either immaterial or made without scienter. We affirm in part, reverse in part, and remand.

BACKGROUND

Apple is a publicly-traded company which manufactures computers and computer peripherals. The individual defendants were officers and directors of Apple at the time of the events complained of — November 12, 1982 through September 23, 1983. During the six months immediately preceding this "class period," Apple's common stock traded in a range of between $11 and $30 per share.

In 1982, Apple was readying a computer named "Lisa" and a compatible disk-drive named "Twiggy" for commercial release. Apple's previous successes, most notably the "Apple II," had been in the home computer market. With Lisa, Apple hoped to service the computer needs of medium-size to large corporations. Lisa contained a number of technological innovations which later proved to be commercially viable when incorporated into the "Macintosh" home computer. For example, Lisa pioneered use of the "mouse" — a hand-held device which allows the operator to communicate with the computer without using the keyboard — and "icons" — graphic displays of the computer's functions. However, Lisa and Twiggy themselves proved to be unsuccessful commercially. Apple replaced Twiggy with another disk-drive system before actual sales of Lisa began. Apple discontinued Lisa altogether shortly after the close of the class period.

The named plaintiffs represent a certified class of persons who purchased Apple stock during the class period. They allege that Apple and its top officers made a number of highly positive statements about Lisa and Twiggy during the class period. For example, on November 29, 1982, Apple issued a press release introducing Twiggy, and claiming that "[I]t represents three years of research and development and has undergone extensive testing and design verification during the past year." In a *Business Week* article published on January 31, 1983, Apple's former Chairman of the Board, Steven P. Jobs, is

quoted as stating: "I don't think we will have any problem selling all the Lisas we can build." In a Wall Street Journal article published on April 14, 1983, Jobs is quoted as stating: "Lisa is going to be phenomenally successful in the first year out of the chute."[1] Plaintiffs attribute volatility in Apple's common stock price to these optimistic statements. Apple's stock price soared during the class period, reaching a high of almost $63 per share, and bottomed out at a bit over $17 per share shortly after the class period when Apple disclosed news of Lisa's disappointing sales.

Plaintiffs claim that Apple's officers recklessly ignored a number of problems with Lisa and Twiggy which tended to undermine their public optimism. First, internal tests conducted by Apple indicated some slowness and unreliability in Twiggy's information-processing capabilities. Second, communications among Apple's insiders revealed concern that Lisa could not be made compatible with the IBM computer products which dominated the office computer market. Third, there was also concern within Apple that independents would not design software for Lisa. Finally, before beginning actual sales, Apple submitted Lisa prototypes for use by potential customers on a trial basis, and for the inspection of industry analysts and the press. As a result of this test-marketing, Apple received generally enthusiastic reports, and built up a backlog of over 10,000 pre-shipment orders. However, the press and many of the targeted customers raised questions about the wisdom of Lisa's proposed $9,995 retail price. In light of these problems, plaintiffs claim that Apple's unqualified optimism was false and misleading, and actionable under Section 10(b) of the Securities Exchange Act and Rule 10b-5 enacted thereunder.

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[1]In all, plaintiffs have identified sixteen statements which they claim to be fraudulent. Each of those statements is considered separately later in this opinion.

Although plaintiffs allege that Apple did not fairly and adequately inform the market abouit Lisa's prospects, many of the risks and underlying problems were widely publicized. For example, the same *Business Week* article which quotes Jobs as stating his belief that Apple would have little trouble selling Lisa also states: "One indication of how uncertain Apple's prospects are is that expert estimates of how many Lisas the company will sell are all over the lot — from 2,000 to 30,000." The article also questions whether independent software writers would support Lisa, and whether the $9,995 price tag was realistic. Similarly the *Wall Street Jouranl* article in which Jobs predicts that Lisa will be "phenomenally successful" is entitled "Some Warm Up to Apple's 'Lisa,' but Eventual Success is Uncertain." The article details Apple's difficulties in achieving IBM compatibility, in attracting independent software suppliers, and in raising consumer interest at $9,995. On the other hand, both articles and many others identified by the parties report positive evaluations of Lisa by many large corporations — a number of which expressed interest in purchasing the machine.

In three separate orders, the trial court granted Apple summary judgment against plaintiffs on their entire case.[2] With respect to two of the alleged misstatements, the court held that there was no genuine issue as to scienter. The court held that the remainder of the statements were either not misleading or immaterial as a matter of law, since the information necessary to make the statements not misleading was adequately reported by the press.

On appeal, plaintiffs argue that the trial court misapplied the standard for materiality in a fraud on the

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[2] *In re Apple Computer Securities Litigation*, 672 F.Supp. 1552 (N.D. Cal.1987); *In re Apple Computer Securities Litigation*, 696 F.Supp. 490 (N.D.Cal.1987); and *In re Apple Computer Securities Litigation*, 690 F.Supp. 872 (N.D.Cal. 1987).

market case. They claim that, notwithstanding the press' attention to Lisa's shortcomings, Apple's omissions were material because a reasonable investor would place greater weight on the opinions of corporate insiders. Plaintiffs also argue that evidence of sales of Apple stock during the class period raises a genuine issue as to the defendants' good faith, and evidence that Lisa would be a commercial failure raises a genuine issue as to whether defendants' optimism had a reasonable basis. Finally, plaintiffs argue that the trial court invaded the province of the jury by either ignoring or discrediting the testimony of plaintiffs' expert that Apple's nondisclosures were material and the evidence of volatility in Apple's common stock price.

STANDARD OF REVIEW

A grant of summary judgment is reviewed de novo. *See e.g., California Architectural Building Products, Inc. v. Franciscan Ceramics, Inc.,* 818 F.2d 1466, 1468 (9th Cir.1987), *cert. denied,* 484 U.S. 1006, 108 S.Ct. 698, 98 L.Ed.2d 650 (1988). We may affirm on any ground supported by the record. *Islamic Republic of Iran v. Boeing Co.,* 771 F.2d 1279, 1288 (9th Cir. 1985), *cert. dismissed,* 479 U.S. 957, 107 S.Ct. 450, 93 L.Ed.2d 397 (1986).

Under Fed.R.Civ.P. 56(c), summary judgment is appropriate where there is "no genuine issue as to any material fact," and the moving party is "entitled to a judgment as a matter of law." This standard "mirrors the standard for a directed verdict under Federal Rules of Civil Procedure (50(a), which is that the trial judge must direct a verdict if, under the governing law, there can be but one reasonable conclusion as to the verdict." *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 250-51, 106 S.Ct. 2505, 2511, 91 L.Ed.2d 202 (1986). "No longer can it be argued that any disagreement about a material issue of fact precludes the use of summary judgment." *California Architectural Building Products,* 818 F.2d at 1468.

The party moving for summary judgment has the "initial responsibility of informing the district court of the basis for its motion, and identifying those portions" of the record showing the absence of a genuine issue of fact. *Celotex Corp. v. Catrett,* 477 U.S. 317, 323, 106 S.Ct. 2548, 2552, 91 L.Ed.2d 265 (1986). The burden then shifts to the nonmoving party to present evidence sufficient to support a verdict in its favor on every element of its claim for which it will carry the burden of proof at trial. *Id.* at 322-23, 106 S.Ct. at 2552-53. "If the [nonmoving party's] evidence is . . . not sufficiently probative . . . summary judgment may be granted." *Anderson,* 477 U.S. at 249-50, 106 S.Ct. at 2511.

Materiality and scienter are both fact-specific issues which should ordinarily be left to the trier of fact. *See Basic, Inc. v. Levinson,* 485 U.S. 224, 108 S.Ct. 978, 982, 985-87, 99 L.Ed.2d 194 (1988); *Vucinich v. Paine, Webber, Jackson & Curtis, Inc.,* 739 F.2d 1434, 1436 (9th Cir.1984) (per curiam). However, summary judgment may be granted in appropriate cases. *See Ross v. Bank South, N.A.,* 837 F.2d 980, 1003 (11th Cir.1988) (affirming summary judgment on issue of scienter in securities fraud case); *Matsushita Electric Industrial Co. v. Zenith Radio Corp.,* 475 U.S. 574, 587, 106 S.Ct. 1348, 1356, 89 L.Ed.2d 538 (1986).

SECTION 10(b) LIABILITY UNDER A FRAUD ON THE MARKET THEORY

Rule 10b-5, enacted under Section (10(b), makes it unlawful "[t]o make any untrue statement of fact or to omit to state a material fact necessary to make the statements made, in light of all the circumstances in which they were made, not misleading." The most obvious example of a false or misleading statement is a misrepresentation of historic fact. The statement that "Apple began volume shipments June One of its new $10,000 Lisa Computer," for example, may be actionable if volume

shipments did not in fact begin until the middle of June, if the inaccuracy is material, and if it was made recklessly or in bad faith. *See, e.g., Bell v. Cameron Meadows Land Co.,* 669 F.2d 1278, 1281 (9th Cir.1982).

Most of the statements challenged by plaintiffs are projections or general expressions of optimism, as opposed to simple representations of historic fact. The "truth" of such statements as the prediction that "Lisa is going to be phenomenally successful" and the assertion that "we are very pleased with the market acceptance and orders to date" presents more subjective issues. Nonetheless, projections and general expressions of optimism may be actionable under the federal securities laws. *See, e.g., Marx v. Computer Sciences Corp.,* 507 F.2d 485, 489-92 (9th Cir. 1974); *G & M Inc. v. Newbern,* 488 F.2d 742, 745-46 (9th Cir.1973). A projection or statement of belief contains at least three implicit factual assertions: (1) that the statement is genuinely believed, (2) that there is a reasonable basis for that belief, and (3) that the speaker is not aware of any undisclosed facts tending to seriously undermine the accuracy of the statement. A projection or statement of belief may be actionable to the extent that one of these implied factual assertions is inaccurate. *Marx,* 507 F.2d at 490.

Plaintiffs bring their claim under the so-called "fraud on the market" theory first recognized by this court in *Blackie v. Barrack,* 524 F.2d 891 (9th Cir. 1975), *cert. denied,* 429 U.S. 816, 97 S.Ct. 57, 50 L.Ed.2d 75 (1976). In the usual claim under Section 10(b), the plaintiff must show individual reliance on a material misstatement. Under the Fraud on the market theory, the plaintiff has the benefit of a presumption that he has indirectly relied on the alleged misstatement, by relying on the integrity of the stock price established by the market. The Supreme Court has recently considered a corporate insider's liability for affirmative misrepresentatives under the fraud on

the market theory. *Basic, Inc. v. Levinson,* 108 S.Ct. 978 (1988). This case raises similar issues with regard to misleading predictions or statements of belief.

Liability for Failure to Disclose Material Risks

The most closely controverted issue in this case is whether the defendants' optimistic statements about Lisa and Twiggy are shielded from liability because of the press' documentation of the relevant risks. The trial court held that disclosures by the press rendered the defendants' omissions immaterial. Ordinarily, omissions by corporate insiders are not rendered immaterial by the fact that the omitted facts are otherwise available to the public. *See, e.g., Hughes v. Dempsey-Tegeler & Co.,* 534 F.2d 156 (9th Cir.1987); *Fisher v. Plessey Co.,* 559 F.Supp. 442, 445 (S.D.N.Y.1983). Where a plaintiff alleges actual reliance on a particular statement, it does not matter that the *market* is aware of the facts necessary to make the statement not misleading. The plaintiff may be misled into believing that the stock has been incorrectly valued by the market.

The situation is different in a fraud on the market case. In a fraud on the market case, the plaintiff claims that he was induced to trade stock not by any particular representations made by corporate insiders, but by the artificial stock price set by the market in light of statements made by the insiders as well as all other material public information. Provided that they have credibly entered the market through other means, the facts allegedly omitted by the defendant would already be reflected in the stock's price; the mechanism through which the market discovered the facts in question is not crucial.

The point is best illustrated by way of example. Assume that only two "facts" are relevant to Lisa's prospects, and assume that both facts are equally "true": (1) Apple's Chairman of the Board believes that Lisa will be phenomenally successful, and (2) a number of potential custom-

ers have balked at Lisa's proposed $9,995 retail price. Where both facts are transmitted to the market with roughly equal intensity and credibility, the market will receive complete and accurate information. Informed investors will invest in light of an accurate appreciation of the relevant risks. Those investors who know only of the Chairman's optimism may overvalue Apple stock; those who know only of the problems with the suggested retail price may undervalue the stock. However, it is a basic assumption of the securities laws that the partially-informed investors will cancel each other out, and that Apple's stock price will accurately reflect all relevant information.[3] Particular individuals who hear only one of the two facts may receive a distorted impression of Lisa, and thus may have an actionable claim. But the *market,* and any individual who relies only on the price established by the market, will not be misled.

In a recent opinion, the Supreme Court has explicitly embraced this line of reasoning. *See Basic,* 108 S.Ct. at 992. In *Basic,* a would-be class of stock holders alleged that corporate insiders fraudulently depressed the price of the corporation's stock by falsely denying that they were engaged in merger negotiations. Defendants opposed class certification on the theory that questions of individual reliance on the alleged misstatements predominated over common questions. The trial court overcame that obstacle to class certification by holding that all members of the putative class were entitled to a presumption that they relied on the stock price established by the market, which in turn reflected the alleged misstatements. The Supreme Court approved the trial

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[3]"Recent empirical studies have tended to confirm Congress' premise that the market price of shares traded on well-developed markets reflects all publicly available information. . . ." *Basic,* 108 S.Ct. at 991. *See In re LTV Securities Litigation,* 88 F.R.D. 134, 144 (N.D. Tex.1980) (citing studies).

court's adoption of the fraud on the market theory. However, it stressed that the presumption of reliance could be rebutted by a showing that information sufficient to correct the defendants' alleged misstatements was transmitted through market price in the same fashion as the misstatements themselves. The Court stated:

> For example, if petitioners could show that the "market makers" were privy to the truth about the merger discussions . . . and thus that the market price would not have been affected by their misrepresentations, the causal connection could be broken: the basis for finding that the fraud had been transmitted through market price would be gone. Similarly, if, despite petitioner's allegedly fraudulent attempt to manipulate market price, news of the merger discussions credibly entered the market and dissipated the effects of the misstatements, those who traded Basic shares after the corrective statements would have no direct or indirect connection with the fraud.

Id.

We conclude that in a fraud on the market case, the defendant's failure to disclose material information may be excused where that information has been made credibly available to the market by other sources. The issue with regard to the bulk of Apple's misstatements is whether, in light of the press' documentation of Lisa's risks, a rational jury could nonetheless find a "substantial likelihood" that full disclosures by Apple would have "significantly altered the 'total mix' of information made available." *TSC Industries, Inc. v. Northway, Inc.* 426 U.S. 438 449, 96 S.Ct. 2126, 2132, 48 L.Ed.2d 757 (1976).

With respect to two of the challenged statements, there are genuine issues of material fact. In a November 29, 1982 press release, Apple stated that Twiggy "ensures greater integrity of data than the other high density drives by way of a unique, double-sided mechanism de-

signed and manufactured by Apple." (Statement 4). Apple also claimed that Twiggy "represents three years of research and development and has undergone extensive testing and design verification during the past year." (Statement 5). At the time these optimistic statements were made, internal tests conducted by Apple indicated slowness and unreliability in Twiggy's information-processing capabilities. Approximately two weeks before the press release was issued, the Apple division responsible for production of Lisa warned top executives that "[a]s of now, the Twiggy reliability would lead us to DELAY THE INTRODUCTION OF LISA BY MANY MONTHS." On December 6, 1982, Steven Jobs expressed "virtually zero confidence" in the division that was responsible for the design and development of Twiggy.

There is at least a triable issue of whether Twiggy's technical problems were material facts tending to undermine the unqualified optimism of Statements 4 and 5. Unlike the information about Lisa's market risks, these problems were not made known to the market by the press or by anyone else. However, the November 29, 1982 press release stated that Twiggy would not be available until the following spring. Apple has produced affidavits from several market experts stating that when a computer industry product is announced for future availability, the market fully understands the product is still in the development stage. Apple therefore claims that the market did not understand Statements 4 and 5 as implying that Twiggy was ready to perform, and that the technical problems Apple was encountering did not materially undermine the optimistic press release.

Whether this argument has merit is a question which should be decided by the jury. The expert affidavits introduced by Apple never state definitively that the market as a whole was aware that there was a problem with Twiggy. There is a difference between knowing that

any product-in-development may run into a few snags, and knowing that a particular product has already developed problems so significant as to require months of delay. We are unable to say as a matter of law that Apple's failure to disclose Twiggy's technical problems had no misleading effect on market price.

The remainder of the challenged statements involved Lisa, or Apple generally, rather than Twiggy. Although many of these statements failed to disclose material risks, we agree with the trial court that there are no genuine issues of fact under a fraud on the market theory. The press portrayed Lisa as a gamble, with the potential for either enormous success or enormous failure. At least twenty articles stressed the risks Apple was taking, and detailed the underlying problems producing those risks. Many of the optimistic statements challenged by plaintiffs appeared in those same articles, essentially bracketed by the facts which plaintiffs claim Apple wrongfully failed to disclose. The market could not have been made more aware of Lisa's risks.

We stress the limits of our holding. Scrutiny by the press will not ordinarily excuse the tye of unqualified exuberance expressed by Apple and its officers in this case. Even in a fraud on the market case, corporate insiders are not relieved of their duty to disclose material information where that information has received only brief mention in a few poorly-circulated or lightly-regarded publications. The investing public justifiably places heavy reliance on the statements and opinions of corporate insiders. In order to avoid Rule 10b-5 liability, any material information which insiders fail to disclose must be transmitted to the public with a degree of intensity and credibility sufficient to effectively counterbalance any misleading impression created by the insiders' one-sided representations. *See Basic*, 108 S.Ct. at 992 (the presumption that a fraudulent statement has been

transmitted through market price may be rebutted by a showing that "corrective statements" have "*credibly* entered the market") (emphasis added). That standard has been met in this case because of the press' intense, sustained focus on Lisa and her risks.

Plaintiffs argue that summary judgment is nonetheless inappropriate because their claim of materiality was supported by evidence of stock price movements, and by the testimony of plaintiffs' expert. The evidence of stock price movement does not raise a genuine issue of material fact. The crucial issue with regard to most of the optimistic statements is whether the statements were misleading because they *omitted* material information. Dramatic price movements in response to an optimistic statement would provide a strong indication that the statement itself was material, but would not suggest that material information tending to undermine the statement has not been made available to the market. An entirely plausible explanation would be that the market was persuaded by Apple's optimism notwithstanding the known risks. In that case, the optimistic statement could still result in liability if the statement was not genuinely believed, or if that belief lacked a reasonable basis. *See Marz,* 507 F.2d at 490-91. But the evidence of stock price movements provides no rational basis for determining whether Lisa's risks were adequately conveyed to the public, and therefore is not enough to get plaintiffs to the jury on the first theory of liability in *Marz.*

More problematic is the testimony by plaintiffs' expert to the effect that the investment community pays special attention to the statements of corporate management and that Apple's nondisclosures were therefore material. As a general rule, summary judgment is inappropriate where an expert's testimony supports the nonmoving party's case. *See, e.g., Bieghler v. Kleppe,* 633 F.2d 531, 534 (9th Cir.1980). However, where the evidence is as clear as that

in this record, the court is not required to defer to the contrary opinion of plaintiffs' "expert." It does not require any special competence to read the pertinent press reports and conclude that Lisa's risks were adequately conveyed to the public.

Scienter

With regard to the great bulk of the statements challenged by the plaintiffs, we have held that the publicity surrounding Lisa was sufficient to shield Apple from liability for failing to disclose material risks. Apple alternatively argues that it is nonetheless entitled to summary judgment because there is no rational basis in the record for concluding that any of the challenged statements was made with the requisite scienter. We have interpreted scienter to include recklessness. *Vucinich,* 739 F.2d at 1435.

Except for statements four and five, we agree with Apple. The significant technological flaws in Twiggy raise a genuine issue of material fact as to these statements' recklessness. However, plaintiffs produced no evidence controverting defendants' good faith basis for making the other statements. Each of Apple's officers filed an affidavit stating that he acted in good faith belief that his optimistic statements were accurate and not misleading. Apple's massive investment in Lisa demonstrates this good faith. Apple's officers also had a reasonable basis for their optimism about Lisa, given the novelty of Lisa's technology, the positive responses Apple had received from its test-marketing and from the press, and the substantial backlog of pre-shipment orders. Plaintiffs contend that much of the evidence available to Apple suggested that Lisa's prospects were bleak. The results of Apple's test marketing, its internal studies, and reports by the press all may have suggested that Lisa was a gamble. But none of these sources suggested that optimism was unrealistic. Granting them every reasonable

inference, plaintiffs can only show that Lisa's prospects were uncertain. Such a showing is insufficient to support liability as a matter of law. *See Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 206, 96 S.Ct. 1375, 1387, 47 L.Ed.2d 668 (1976) (a defendant may not be found liable under Rule 10b-5 "unless he acted other than in good faith").

Plaintiffs also point to evidence that defendants collectively sold about 8% of their Apple holdings valued at roughly $84 million during the class period. Plaintiffs claim that these sales are inconsistent with Apple's expressed optimism, and raise a genuine issue as to the defendants' good faith. Insider trading in suspicious amounts or at suspicious times is probative of bad faith and scienter. *See, e.g., Goldman v. Belden,* 754 F.2d 1059, 1070 (2d Cir.1985). However, the pattern of stock trading by Apple's insiders is insufficient to raise an issue for the jury. The defendants collectively sold a slightly greater number of shares during an equal period of time just before the class period than they did during the class period. Uncontradicted disposition testimony from several of the defendants provided credible and wholly innocent explanations for the stock sales, ranging from long-standing programs of periodic divestment, to the need to free cash to meet matured tax liabilities. These unrebutted explanations are sufficient to defeat any inference of bad faith. *See Freeman v. Decio,* 584 F.2d 186, 197 n. 44 (7th Cir.1978) (inference that defendants were acting in bad faith "can be nullified by a showing that sales in question were consistent in timing and amount with a past pattern of sales or that other circumstances might reasonably account for their occurrence") (affirming grant of summary judgment on issue of scienter).

Plaintiffs finally focus on an episode of trading in the month immediately preceding the class period. During this time, the defendants sold roughly as much stock by

share as they sold in the preceding 10 months, and roughly half as much as they sold during the class period. Plaintiffs argue that this trading blip — for which a single defendant was primarily responsible — raises an inference that defendants had become aware shortly before announceing Lisa to the public that Lisa would probably be a failure. We cannot agree. Large sales of stock *before* the class period are inconsistent with plaintiffs' theory that defendants attempted to drive up the price of Apple stock *during* the class period. As sophisticated investors, defendants must have known that pre-class period sales would deprive them of much of the value of their "false" optimism. Those cases basing a finding of bad faith on insider trades have involved trades in amounts dramatically out of line with prior trading practices at times calculated to maximize personal benefit from undisclosed inside information. *See, e.g., Lilly v. State Teachers Retirement System,* 608 F.2d 55, 56 (2d Cir.1979) *cert. denied,* 446 U.S. 939, 100 S.Ct. 2159, 64 L.Ed.2d 792 (1980) (sale of 80,000 shares nine days prior to public announcement that "problem loans" had increased from $7 million to $16 million); *SEC v. Musella,* 578 F.Supp. 425, 441 (S.D.N.Y.1984) (multiple episodes of stock trades within days or weeks of "public announcements having a significant market impact on the value of the securities"); *Jefferies & Co. v. Arkus-Duntov,* 357 F.Supp. 1206 (S.D.N.Y.1973) (sale of 40,000 shares two days before the SEC suspended trading in the stock). The pre-class period sales were so inauspiciously timed that a jury would have little or no justification in inferring that they were motivated by the belief that Lisa would be a failure.

Any remote inference of bad faith arising from the defendants' stock sales is completely dispelled by the defendants' overall pattern of conduct. Throughout the class period, the defendants continued to stake much of Apple's future on the success of Lisa, pouring millions of

dollars into product development, market research, and promotions. At the same time, defendants retained the great bulk of their Apple holdings, and held on in the face of a decline in value of almost 75% following disclosure of Lisa's disappointing sales. The most that can be said of the evidence in this case is that while defendants bet quite heavily on Lisa, they did not put *all* of their eggs in the same basket. We cannot conclude that this conduct is so inconsistent with the defendants' expressed optimism as to raise a triable issue regarding the defendants' good faith.

THE STATEMENTS

Plaintiffs argue that the trial court erred by considering each of the challenged statements in isolation, rather than looking to the overall pattern of deception carried out by Apple. As we have discussed, any overall impression created by Apple's optimism was adequately counterbalanced by the press' documentation of Lisa's risks. Plaintiffs may defeat summary judgment only by showing a genuine issue of fact with regard to a particular statement by Apple or its insiders. Except with regard to the statements about Twiggy, plaintiffs have failed to meet this burden.

Statements 1, 2 and 3. The first three statements appeared in Apple's 1982 Annual Report, issued on November 12, 1982. Defendants Jobs and Markkula boast of Apple's "unequalled strength, experience and expertise," and announce that a "significant breakthrough," Lisa, will be introduced in 1983. (Statement 1) Another employee opines: "From all I've seen so far, success should continue." (Statement 2) Apple reports that its forecasting process had been "refined." (Statement 3). There were sound historical and factual bases for each of these statements. At the time the statements were made, Apple had established a successful track record, and there were no indications that this success would not continue. Lisa

was a promising, innovative product-in-development. Apple had recently refined its planning process. A rational jury could not find these statements materially misleading. The 1982 Annual Report contained frank admissions regarding the uncertainties in the computer industry.

Statements 4 and 5. We have already considered Statements 4 and 5. There is evidence in the record from which a jury could conclude that Apple was aware of significant technical problems with Twiggy, which it did not disclose and which were not otherwise made known to the market, and which tended to materially undermine Apple's stated optimism. This evidence is enough to raise an issue for the jury.

Statements 6, 7, 8 and 9. The next four statements all appeared in press reports between January and April of 1983. Various of the defendants make the following assertions: "Lisa incorporates the latest software and hardware technology." (Statement 6); "I don't think we will have any trouble selling all the Lisas we can build." (Statement 7); "Lisa is going to be phenomenally successful the first year out of the chute." (Statement 8); and "[Lisa] is going to make Apple's growth before this look small." (Statement 9) Each of these general expressions of optimism was made in the context of a barrage of publicity regarding Lisa's riskiness. There is no genuine issue under a fraud on the market theory.

Statement 10. In an April 14, 1983 Wall Street Journal article, an Apple employee is quoted as stating: "We find people willing to put down $10,000 without blinking an eye," and "more companies are willing to commit themselves to larger orders that Apple has expected." At the time this statement was made, Apple had a pre-shipment backlog of over 10,000 Lisa orders. Plaintiffs argue that the statement is nonetheless misleading because Apple failed to disclose that customers could cancel these pre-shipment orders without penalty. However, Apple intro-

duced unrebutted testimony from four securities analysts that it was well understood within the investment community that computer orders are "soft." The analysts further testified that the market understood that the backlog of Lisa orders was soft, and that Statement 10 was received in that light. Plaintiffs have raised no genuine issue regarding whether Apple's failure to disclose the softness of Lisa orders misled the market. A jury could not find Apple liable under a fraud on the market theory.

Statements 11, 12, 13, 14 and 16. In Statements 11-14 and 16, various of the defendants express satisfaction with the early market reception of Lisa: "We are extremely pleased with the market acceptance and orders to date." (Statement 11); "The acceptance of Lisa among accounts has been very strong." (Statement 12); "The interest by individuals at the dealer level has surprised us." (Statement 13); "[Lisa orders] are double what had been anticipated." (Statement 14); and "[W]e remain pleased with [Lisa's] market acceptance, order rate and dealer enthusiasm. Lisa is clearly being recognized as an important force in the office market." (Statement 16). Statements 11-14 were all made before actual sales of Lisa began. In light of a pre-shipment backlog of over 10,000 orders, no rational jury could find that these statements lacked a reasonable basis. Although Statement 16 was made shortly after sales of Lisa had begun, the claim that Lisa is being recognized as an "important force" was not undermined by any nonpublic information available to Apple at the time. Lisa sales did not begin to dip below those forecasted in Apple's 1983 Business Plan until after Statement 16 was issued.

Statement 15. In Statement 15, an Apple employee assets that volume shipments of Lisa began on June 1, 1983, when they did not in fact begin until later that month. Although the trial court ultimately found this misstatement material, plaintiffs have made no showing

that a reasonable investor would regard the two-week error as significant. In addition, plaintiffs have produced no evidence that the statement was anything other than an honest mistake. Summary judgment is appropriate on either materiality or scienter grounds.

CONCLUSION

Plaintiffs have raised genuine issues of material fact in support of their claims that the optimistic statements about Twiggy were materially misleading. We remand so that plaintiffs can present these claims to a jury. However, there are no triable issues with regard to the remainder of plaintiffs' claims. Defendants have conclusively established that all material information tending to undermine their optimistic statements about Lisa had credibly entered the market. There is no rational basis for concluding that the defendants did not genuinely and reasonably believe that these statements were accurate. The trial court properly granted summary judgment.

Each party shall bear its own costs on appeal.

AFFIRMED IN PART, REVERSED IN PART, AND REMANDED.

APPENDIX

B

[672 F. Supp. 1552]

In re APPLE COMPUTER SECURITIES LITIGATION.

No. C 84-20148(A) RPA.

United States District Court,
N.D. California,

April 30, 1987
as amended Oct. 19, 1987.*

AMENDED ORDER GRANTING IN LARGE PART DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

AGUILAR, District Judge.

I. INTRODUCTION

The Court has been inundated with paper in connection with this motion. Hundreds of pages of briefs and thousands of pages of documents have flooded this Court as plaintiffs struggle to avoid the pains of summary judgment. Two "simple issues" — those of materiality and scienter — lie at the center of conflict. After much careful deliberation and analysis, the Court finds that the majority of plaintiffs' case cannot withstand this motion. As to scienter, the Court will find that there are triable issues of material fact still in dispute which preclude the entry of summary judgment. However, fourteen of the sixteen statements which form the basis of plaintiffs' case are either not misleading or are not material. Therefore, as to these fourteen statements, the Court will grant summary judgment in favor of defendants. The remaining

*The April 30, 1987 Order was revised for publication on October 19, 1987.

two statements constitute all that is left of plaintiffs' case.

II. FACTS

The facts are both straightforward and somewhat complicated. The complicated aspect will be analyzed below. A simple rendition of the facts begins with the identification of the plaintiffs, a certified class of investors (hereafter the "class") who purchased stock in Apple Computer, Inc. ("Apple") during the period November 12, 1982 to September 23, 1983 (hereafter the "class period"). At the beginning of the class period, Apple stock sold for approximately $32 per share. During the class period, Apple stock reached a high of approximately $63 per share (in June 1983). On the final day of the class period, after Apple announced a sharp decline in expected profits for the fourth quarter of 1983, the company's stock plummeted to a class period low of approximately $24 per share. Despite the upward swing in value during the class period, the net decline in the value of Apple stock from $32 to $24 per share actually can be accounted for in a single day. On September 23, 1983, the stock declined 25% from $32 to $24 per share.

Apple is a major manufacturer of micro-processor-based personal computer systems with its headquarters in Cupertino, California. Apple products such as the Apple II, Apple III, Lisa, and MacIntosh microcomputers have generated hundreds of millions of dollars of sales worldwide. As of the time of the filing of the amended class action complaint, apple reportedly had outstanding some 57 million shares of common stock which are listed to trade and actively have been traded since 1981.

The class is suing the directors and top level executives of Apple for violation of the securities laws. Specifically, plaintiffs sue under § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78(j), and rule 10b-5 of the regulations of the Securities Exchange Commission, 17

C.F.R. § 240.10b-5 (1987). Plaintiffs allege that defendants recklessly, or perhaps knowingly, made misstatements and omissions of material fact with respect to the sale of the Apple "Lisa" computer.

The Lisa computer was introduced to the public on January 19, 1983. As pointed out by Apple, Lisa incorporated several innovations that significantly facilitated its use. Among these innovations were: the "Mouse," a handheld controller that allowed communication with the computer without using the keyboard; "icons," pictorial representations of different computer functions displayed on the screen that enabled the user to execute commands using the Mouse; and six integrated software applications that accelerated learning. Apparently all three of these features are now widely used in the industry.

Plaintiffs allege that they relied on misstatements and omissions made by Apple officials relating to the Lisa computer and were injured as a result. Plaintiffs' argument is summarized in the following passage from their brief in opposition to this motion:

> Defendants, Apple and its key officers and directors, knew throughout the November 12, 1982 — September 23, 1983 class period that several serious problems were crippling their efforts to develop and manufacture Lisa and impairing Lisa's bid for market acceptance. Despite this knowledge, or in reckless disregard of facts easily accessible to all defendants, Apple issued a series of positive but false statements to the business and financial marketplace which inflated its stock price until the truth began to be revealed at the end of the class period, on September 23, 1983.

Plaintiffs' Memorandum in Opposition to Apple Computer's and the Officer Defendants' Motion for Summary Judgment at 2-3 (hereafter "*Opposition Brief*"); *see also* plaintiffs' *Consolidated Amended Class Action Complaint For Viola-*

tion of federal Securities Laws at 2-3 (hereafter the "*Complaint*").

The two groups of defendants, the "inside" and "outside" directors, have brought motions for summary judgment asserting that plaintiffs (1) have not demonstrated that the alleged misstatements are anything other than the informed and sincere (but erroneous) opinions of apple officials and (2) have not rebutted defendants' sworn affidavits to the effect that each and every one of them acted honestly and in good faith in making any statements referring to the Lisa computer. The motions will be treated as a single motion for purposes of discussion herein. The task for the Court in this motion is to determine whether plaintiffs have succeeded in establishing the existence of any triable issue of material fact. If defendants can succeed in winning summary judgment on either materiality or scienter, plaintiffs' entire complaint fails.

III. MATERIALITY

(A) *Legal Standards:*

The Ninth Circuit has adopted an objective test for materiality. *Caravan Mobile Home Sales v. Lehman Bros. Kuhn Loeb,* 769 F.2d 561, 565 (9th Cir. 1985). the test is "whether there is a substantial likelihood that a reasonable investor would consider the fact important in making an investment decision." *Id., quoting Vaughn v. Teledyne, Inc.,* 628 F.2d 1214, 1221 (9th Cir.1980). this test is drawn from the Supreme Court's opinion in *TSC Industrirs, Inc. v. Northway, Inc.,* 426 U.S. 438, 96 S.Ct. 2126, 48 L.Ed.2d 757 (1976). After articulating a "reasonable investor" standard in *TSC,* the Court went on to explain that the standard:

> [D]oes not require proof of a substantial likelihood that disclosure of the omitted fact would have caused the reasonable investor to change his [behavior].

> What the standard does contemplate is a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable [investor]. Put another way, there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of information made available.

Id. at 449, 96 S.Ct. at 2132; *see also Grigsby v. CMI Corp.*, 765 F.2d 1369, 1372-73 (9th Cir.1985) (quoting above text from *TSC*). The definition of materiality is the same whether misrepresentations or omissions are involved. *Kramas v. Security Gas & Oil Inc.*, 672 F.2d 766, 769 (9th Cir.1982), *cert. denied,* 459 U.S. 1035, 103 S.Ct. 444, 74 L.Ed.2d 600.

The standard for granting summary judgment is fixed by Rule 56(c) of the Federal Rules of Civil Procedure ("Fed.R.Civ.P."). Summary judgment is proper only when (1) the pleadings, affidavits, and other supporting papers permitted by Rule 56(c) demonstrate that there is no disputed issue of material fact, and (2) the moving party is entitled to prevail as a matter of law. Fed.R.Civ.P. 56(c); *Celotex Corp. v Catrett,* 477 U.S. 317, 106 S.Ct. 2548, 2552-54, 91 L.Ed.2d 265 (1986); *Admiralty Fund v. Hugh Johnson & Co.,* 677 F.2d 1301, 1305-06 (9th Cir.1982).

In the context of a motion for summary judgment in a 10b-5 action, courts have been admonished to proceed with great care. Consisting as it does in the application of purportedly objective legal standards to a constellation of facts, the task of assessing materiality is clearly a mixed question of law and fact. The Supreme Court has instructed that the underlying objective facts "are merely the starting point" for the ultimate determination of

materiality. *TSC*, 426 U.S. at 450, 96 S.Ct. at 2133. In the Court's words, the determination requires:

> [D]elicate assessments of the inferences a "reasonable shareholder" would draw from a given set of facts and the significance of those inferences to him, and these assessments are peculiarly ones for the trier of fact. Only if the established omissions are "so obviously important to an investor, that reasonable minds cannot differ on the question of materiality" is the ultimate issue of materiality approximately resolved "as a matter of law" by summary judgment.

Id., quoting Johns Hopkins University v. Hutton, 422 F.2d 1124, 1129 (4th Cir.1970).

Consistent with the Supreme Court's analysis in *TSC*, the Ninth Circuit has adopted rigorous standards for ruling on summary judgment motions in cases of securities fraud. Summary judgment is normally inappropriate for determining the materiality of undisclosed information, *Caravan Mobile Home*, 769 F.2d at 565, nor for determining the materiality of potentially misleading information. *See Admiralty Fund v. Hugh Johnson & Co.*, 677 F.2d 1301, 1306 (9th Cir.1982). A district court should not decide a case of this nature on a motion for summary judgment "unless the court has engaged in meticulous and well articulated analysis of each item of withheld or misrepresented information." *Admiralty Fund, id.* at 1306, and "unless reasonable minds could not differ on the determination of the materiality of the withheld [or misleading] information." *Caravan Mobile Home Sales*, 769 F.2d at 565.

Thus, as the moving party, the defendants here have the onerous burden of showing that no reasonable person could conclude that the information disseminated or allegedly withheld by the defendants was material. In other words, the information at issue did not and would not have "assumed actual significance in the deliberations of

the reasonable shareholder." *TSC,* 426 U.S. at 449, 96 S.Ct. at 2132. This burden is intensified by the rule that the Court must view all fact and inferences from the facts presented in the light most favorable to the plaintiffs, the non-moving parties. *Western Reserve Oil & Gas Co. v. New,* 765 F.2d 1428, 1430 (9th Cir.1985), *cert. denied,* 474 U.S. 1056, 106 S.Ct. 795, 88 L.Ed.2d 773 (1986).

(b) *Theory of the Case:*

[7] Plaintiffs' theory of the case is relevant to how this Court will assess the issue of materiality. Plaintiffs' theory is stated succinctly in § 45 of the Complaint:

> As a result of the foregoing [actions by defendants], the market price of Apple common stock was artificially inflated during the Class Period. In ignorance of the false and misleading nature of the representations described above, plaintiffs and other members of the Class relied, to their damage, on the integrity of the market as to price.

Plaintiffs' theory is commonly known as the "fraud on the market" theory of recovery. The crux of the theory is that the "integrity" of the market was distorted due to the defendants' material misstatement or omissions. As a result of the distortion, plaintiffs purchased the inflated stock during the class period and were damaged when the misrepresentations came to light thereby causing the inflated stock to plummet in price. *See* Note, "the Fraud-On-The-Market Theory," 95 *Harv. Le.Rev.* 1143 (1982); *Shapiro v. Merrill Lynch & Co.,* 634 F.Supp. 587, 596 (S.D. Ohio 1986).

The validity of the fraud on the market theory in this circuit was established in the case of *Blackie v. Barrack.* 524 F.2d 891 (9th Cir.1975). The virtue of this theory, as the court explained in *Blackie,* is that it obviates the reliance requirement under Rule 10b-5 by allowing a plaintiff to recover simply by showing "the causal connec-

tion between the defendant's wrongdoing and the plaintiff's loss." *Id.* at 906. Hence, under *Blackie,* a plaintiff may state a case for liability by showing his purchase of a security and a material misrepresentation or omission by the defendant. *Id.; see also Beebe v. Pacific Realty Trust,* 99 F.R.D. 60, 68 (D.Or.1988) (discussing *Blackie*).

Although causation remains a necessary element to recover under a fraud on the market theory, the court in *Blackie* found that proof of "materiality directly establishes causation more likely than not. . . ." 524 F.2d at 906 n. 22. The rationale for such a view is that "a person who trades during the period in question may be harmed by a deception that affects prices and conditions in the relevant market, regardless of whether or not he has relied upon or even heard the deception." *Little v. First California Co.,* 532 F.2d 1302, 1304 n. 3 (9th Cir.1976), *quoting* Note, "The Reliance Requirement in Private Actions Under SEC Rule 10b-5," 88 *Harv.L.Rev.* 584, 592-93 (1975). Thus, this circuit has concluded that "causation in an open market situation consists in showing that deception affected the market and that damage to the plaintiff resulted." *Little,* 532 F.2d at 1304 n. 3, *citing Blackie,* 524 F.2d at 906.

(C) *The Parties' Characterizations:*

At first glance, plaintiffs and defendants appear to be aboard two different ships passing in the night in their arguments concerning the proper interpretation of the materiality standard in a fraud on the market theory case. On the one hand, plaintffs argue the hard line that under Rule 10b-5, "[a] duty to speak the full truth arises when a defendant undertakes to say anything." *First Virginia Bankshares v. Benson,* 559 F.2d 1307, 1317 (5th Cir.1977), *cert. denied,* 435 U.S. 952, 98 S.Ct. 1580, 55 L.Ed.2d 802 (1978); *see also Levinson v. Basic Inc.,* 786 F.2d 741, 747 (6th Cir.1986) (quoting *Virginia Bankshares*), *cert. granted,* ____ U.S. ____, 107 S.Ct. 1284, 94 L.Ed.2d 142.

According to plaintiffs, if a defendant says "X" and plaintiff knew that "not X" was the truth, plaintiff would be entitled to rely upon the defendant and sue the defendant if plaintiff was damaged as a result of relying on the statement "X."

In contrast to plaintiffs, defendants argue that in a fraud on the market case, a defendant's liability for misstatements or omissions is limited to those material facts not already known in the market. Thus even if defendant said "X" knowing that "not X" was true, the statement would not be actionable if the fact of "not X" was known to the market. Pushing the perfect market theory to the limit, defendants suggest that even lies are not actionable provided the truth is available in the market.

After reviewing the pertinent law, the Court concludes that of the two ships in the night, defendants have boarded the proper vessel, although their description of the vessel is somewhat exaggerated. The Court is in agreement with the Seventh Circuit in concluding that in a fraud on the market case, "not every fact must be disclosed." *Teamsters Local 282 Pension Trust Fund v. Angelos,* 762 F.2d 522, 529 (7th Cir.1985); *see also Proimos v. Fair Auto. Repair, Inc.,* 808 F.2d 1273, 1277 (7th Cir.1987) ("The materiality of a statement or omission depends on [its] context."). Indubitably, the duty to disclose referred to in Rule 10b-5 is only triggered when disclosure is necessary "to make the statements made, in the light of the circumstances under which they were made, not misleading." 17 C.F.R. § 240.10b-5(b). In the context of the fraud on the market theory in which the circumstances involve the entire market, this Court is not prepared to assume a perfect market (as defendants would have) or blind investors (as plaintiffs would have). Instead, the Court simply will employ the existing standard articulated by the Supreme Court in *TSC.* Specifi-

cally, disclosure is only required if the omitted fact "would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." 426 U.S. at 449, 96 S.Ct. at 2132. In other words, the focus is not per se upon what was known in the market, but rather upon what effect the disclosure would have had on the market, i.e., would it significantly have altered the "total mix" of information. Therefore, if the information to be disclosed is already known, it probably cannot be considered material. *See Teamster Local 282,* 762 F.2d at 529. With these standards and principles in mind, the Court now turns to the facts surrounding materiality.

(D) *Facts of Materiality:*

The gravamen of the class action complaint focuses on a series of positive public statements made by officers and directors of Apple. The statements were made in annual and quarterly reports to shareholders, as well as news interviews and periodicals, and contained positive representations about Apple, its finances and management, and the design, development, and introduction of the Lisa computer system. Plaintiffs contend that these statements were materially false and misleading and operated to artificially inflate the market price of Apple common stock. A sampling of the allegedly false statements includes assertions by Apple officials that the company was designing, manufacturing, and introducing a "revolutionary" and "phenomenally successful" new Lisa computer system that would "make Apple's growth before this look small," and that Apple was pleased with orders for the Lisa computer system which was being recognized as a major force in the office market. Plaintiffs contend that these statement were false because, in fact, Apple was undergoing difficult times as a whole and faced serious problems with Lisa. With respect to Lisa, plaintiffs argue that Apple did not have an adequate marketing plant or

staff to sell large volumes of Lisa, that Lisa was incompatible with other microcomputer systems (including other Apple computers), that Lisa could not communicate with IBM and other mainframe computers, that Lisa did not have adequate software, that the final development and initial manufacture of the software was a debacle, and that Lisa suffered poor sales, cancelled back orders, and general rejection by important sectors of the targeted market.

At the outset, the Court finds that the claims of falsity with respect to the prospects of Apple overall are without merit. An examination of the record reveals that Apple's profits in fiscal 1983, i.e., September 25, 1982 to September 25, 1983, were *higher* that in any of the three prior fiscal years. To wit, in fiscal 1983, Apple earned $1.28 per share; in fiscal 1982 Apple earned $1.06 per share; in fiscal 1981 Apple earned $0.70 per share; and in fiscal 1980 Apple earned $0.24. As noted earlier, the entire drop in value of apple stock during the class period took place on one day, September 23, 1983, when Apple common stock dropped from $32 to $24 per share. The fact is that Apple *remained* a very successful company throughout the class period and any statements to that effect were true. Furthermore, any statements to the effect that Apple would enjoy greater success in 1983 than in any prior year proved to be correct.

Thus, the real issue in this case is whether the hype surrounding Lisa was so inflated as to be false or so exaggerated as to impose a duty on the officers to supplement their statements with negative facts in order to avoid the misleading effect of their positive statements. The parties agree that this issue is at the center of the dispute. Plaintiffs describe their case in the following fashion:

> Defendants have mischaracterized this [case] by asserting that "plaintiffs' complaint is about the

> wisdom of Apple business judgments." This is not true. At issue are defendants' *public statements*, and whether or not they were misleading. (emphasis supplied).

Opposition Brief at 78.

> Similarly, defendants state that:
>
> Plaintiffs' case depends fundamentally on the materiality of defendants' affirmative expressions of optimism about Lisa because those statements allegedly created a duty to disclose adverse information.

Defendants' Reply memorandum In Support of Motion For Summary Judgment (hereafter "*Reply Brief*") at 39.

Thus, there is no dispute that this motion focuses on statements made by Apple officers which plaintiffs say were misleading and defendants contend were merely "puffing." After careful consideration of relevant precedent and a review of all the papers relating to the supposed omissions, the Court funds that plaintiffs have not demonstrated that tnere is a "genuine issue for trial" on the question of materiality with respect to fourteen of the sixteen statements at issue. Fed.R.Civ.P. 56; *see also Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 106 S.Ct. 1348, 1356, 89 L.Ed.2d 538 (1986). In other words, on the basis of the record taken as a whole, "the evidence is such that a reasonable jury could [not] return a verdict for the non-moving party." *Anderson v. Liberty Lobby*, 477 U.S. 242, 106 S.Ct. 2505, 2510-12, 91 L.Ed.2d 202 (1986); *Matsushita*, 106 S.Ct. at 1356 ("Where the record taken as a whole could not lead a rational trier of fact to find for the non-moving party, there is no genuine issue for trial."); *First National Bank of Arizona v. Cities Service Co.*, 391 U.S. 258, 289, 88 S.Ct. 1575, 1592, 20 L.Ed.2d 569 (1968).

As the above discussion demonstrates, the Court is cognizant of the fact that materiality is largely a factual

issue that is ill-suited for summary adjudication. Nevertheless, the Court finds that no reasonable minds could differ on the conclusion that the statements made by the defendants, when viewed with an appreciation for the context in which they were made, do not amount to actionable violations of the federal securities laws. In support of this conclusion, the Court offers the following analysis of the context and the specifics of the alleged misstatements and omissions.

(E) *Alleged Misrepresentations:*

Plaintiffs have condensed into several pages a list of some sixteen (16) "positive representations" which they allege constitute actionable violations of § 10(b) and Rule 10b-5. The Court will examine each of these statements in turn as they appear in plaintiffs' brief.

STATEMENT #1:

On November 12, 1982, Apple issued its 1982 Annual Report. Included in the report was a letter by defendants Steven Jobs (Chairman of the Board of Directors and a Vice President) and A.C. Markkula, Jr. (Director and, from 1981 through April 30, 1988, President and Chief Executive Officer) stating the following:

> Apple possesses unequalled strength, experience and expertise in the development, manufacture, marketing and support of personal computer systems. It is a form of equity accumulated during six years devoted exclusively to personal computing. Our ability to concentrate our resources on a single business has solidified our leadership and will sustain our market position in this important growth industry. Several major products resulting from this effort will be announced in calendar 1983. . . . A significant breakthrough in personal office systems will be among these introductions, aimed at professionals, manag-

> ers and administrators within medium- to large-sized corporations.

The bulk of this statement is plain business hype, the kind of pat on the back, "aren't we great" egotism that characterizes much of corporate America. This type of pride and confidence no doubt is partly responsible for Apple's success. More importantly, such boasting clearly is an expression of opinion. In *Apple's view,* Apple is the strongest, the most experienced, the market leader. As this circuit has stated, "[u]nder the securities law a reasoned and justified statement of opinion, one with a sound factual or historical basis, is not actionable." *G & M Inc. v. Newbern* 488 F.2d 742, 745-46 (9th Cir.1973); *see also Hughes v. Dempsey-Tegeler & Co., Inc.,* 534 F.2d 156, 177 (9th Cir.1976), *cert. denied,* 429 U.S. 896, 97 S.Ct. 259, 50 L.Ed.2d 180 (finding general statements of opinion not actionable). In light of Apple's past success and present spiraling growth, there were sound historical and sound factual bases for this opinion.

With respect to the latter half of the statement concerning "a significant breakthrough," this is more than simply hype because it suggests the development of a specific product. If one assumes that the referenced "breakthrough" is the Lisa, then there was a sound factual basis for the statement. At the time Jobs and Markkula wrote, Lisa showed great promise. Indeed, Lisa had great promise, but Apple simply was not able to bring the promise to physical reality in time. As defendant John Sculley (President and Chief Executive Officer beginning May 1, 1983) admitted on November 7, 1983:

> Lisa is a great product, but in hindsight, it was prematurely introduced without datacom, . . . without a broad dealer base for distribution, without a system of work-server accessories, and without a tool kit for software developers.

Taken as a whole and considered in historical context, Statement # 1 does not constitute a misstatement of material fact, nor does it create the need for the disclosure of additional information in order not to be misleading.

STATEMENT #2:

Plaintiffs also point to a second statement made in the 1982 Annual Report of November 12, 1982, as an actionable misstatement. Defendant Arthur Rock stated:

> From all that I've seem so far, success should continue.

The statement was made in the context of a three paragraph blurb in which Rock stated his optimism about the coming year. Plaintiffs do themselves a disservice by referring to this statement, for seen in context, it is obviously a fair and reasoned statement of opinion. Moreover, the rest of the blurb contains frank admissions about the industry and Apple. What is most relevant in relation to Statement #2 is the following disclosure which preceded Statement #2 in Rock's interview:

> To me, so far as Apple in concerned, the main accomplishment of 1982 was management's ability to resolve the problems of the Apple III. To remove a key product from the market, re-engineer it, assure quality and successfully re-introduce it shows that management is in charge of its business. They're not young amateurs who can only feed on success. They can take the hard knocks, come back and do well.

To the reasonable investor, this disclosure probably would generate several inferences. First, Rock is admitting that Apple made some errors in judgment with regard to Apple III; in particular, at the time of its introduction, the computer was ill-equipped to satisfy consumer needs. Second, despite this flaw, Apple management was adept enough to take a product which was

already on the market and successfully re-engineer and re-introduce it while still satisfying consumers. Third, this type of flexibility demonstrates that Apple has and can succeed in spite of adversity. Fourth, on the basis of that very recent experience, Rock believed that even in the face of serious "problems," Apple management had demonstrated that it would guide the company to success. Seen in proper context, then, Statement #2 had a sound historical and factual basis and as such is not actionable under § 10(b) or Rule 10b-5.

STATEMENT #3:

A third statement taken from the 1982 Annual Report is also cited by plaintiffs:

> Apple refined its planning process in 1982, adopting a methodology consistent with company-wide operations. The process is based on a quarterly update program, during which changes from previous plan expectations can be communicated and acted upon as needed.

Plaintiffs have introduced no evidence to suggest that this statement is factually incorrect. Therefore, the Court will assume that Statement #3 is a factually correct representation simply indicating that Apple had refined its planning process. It appears that this was a prudent move in light of a report of May 24, 1982, in which defendant Markkula states that all would agree that the company's forecasts had two important shortcomings. In particular, Markkula reported that "[t]he accuracy of our forecasts, although much improved, is still not good enough." Plaintiffs' Exh. 53 at 508. Subsequently, Apple did introduce changes in its method of forecasting, drawing on the ideas generated in Markkula's May 24, 1982 report. These improvements were then referenced as Statement #3 in the 1982 Annual Report. The Court is unable to find anything false or misleading about Statement #3 because it is an unadulterated report of fact.

A final comment on Statement #3. Plaintiffs apparently contend that Statement #3 was misleading because in fact the forecasting method turned out to be a flop. Cases are legion to the effect that 20-20 hindsight in securities cases is equivalent to Monday morning quarterbacking — enjoyable but nonproductive. In this case, plaintiffs point to a statement of June 1983 attributed to Dave Kinser (apparently Apple's Controller) which, in pertinent part, admitted that "[t]he problem of not being able to scientifically analyse (sic) the backlog remains with us." *Opposition Brief* at 41. Another Apple executive reported on July 15, 1983, that:

> We are being too optimistic about current business trends. Our sales forecasting process is not working. This has serious implications on our inventory and expense controls.

Opposition Brief at 41.

Obviously these statements cannot be used to question the veracity of Statement #3 which was made over half-a-year earlier. These reports do bear on scienter and relate to the next section of this opinion, but they do not go to establish the fraudulent or reckless nature of Apple's expression of its renovated forecasting techniques.

STATEMENTS #4 and #5:

Statements #4 and #5 may be taken together because they both are drawn from the same press release of late November 1982 and relate to the same topic, Apple's new Unifile/Duofile (hereafter "Twiggy") disc drive. The statements are as follows:

> #4 Two high-density floppy disk products which provide new mass storage options for the Apple III personal computer were introduced today by Apple Computer, Inc. The Apple drives ensure greater integrity of data than other high-density drives by way

> of a unique, double-sided mechanism designed and manufactured by Apple.
>
> #5 The Apple 871 Disk Drive [Twiggy] is the first high-density, double-sided disk drive mechanism to be built specifically for personal computer applications. It represents three years of research and development and has undergone extensive testing and design verification during the past year.

Plaintiffs assert that these positive statements about Twiggy disk drive were "premature, without reasonable basis, and materially misleading." *Opposition Brief* at 58. There is no doubt that Twiggy was a serious failure for Apple, but plaintiffs do not appear to challenge the truth of Statement #4 and #5. The question is whether the statements were misleading and therefore obligated defendants to provide fuller disclosure of the status of the Twiggy disk drive.

With respect to Statement #4, the Court is unable to find the statement misleading. It merely reports that the Twiggy is being introduced to the market and that it possesses a unique quality that sets it apart from other disk drives.

The same cannot be said of Statement #5. In this statement, Apple represents that it has invested a great deal of time and effort into developing Twiggy. The reasonable investor would infer from this that Twiggy was a product that was ready to perform. On this point, the investor was misled, because at that time Twiggy was far from ready to perform. In a memo dated November 12, 1982, i.e., two weeks before the issuance of Statement #5, an internal memo prepared by defendant John Couch (Vice President and General manager of Personnel) and circulated to upper echelon apple officials warned:

> We are extremely concerned over the results of our latest run of Twiggy tests. As of 11/12, [November 12, 1982] the current production units show a very

> high failure rate with unknown mode. The current units will show a very high out of box failure rate and we suspect most of them will fail during the warranty period. This level of problems is frightening, considering we are building shipable (sic) Lisas beginning in December.

The Court finds this type of information would have altered the total mix of information available at the time Statement #5 was issued. Given the arguable misleading nature of Statement #5, it may have been incumbent on defendants, once they made this positive statement about Twiggy, to provide an accurate picture of the status of the disk drive so as to avoid misleading investors. At any rate, this is a close jury question which is inappropriate for resolution by summary judgment. Therefore, the Court will deny summary judgment with respect to Statement #5 relating to the Twiggy disk drive.

STATEMENT #6:

Statement #6 is taken from the press release on January 19, 1983, in which Lisa was introduced to the public. The objectionable statement is the following:

> Lisa incorporates the latest software and hardware technology. . . . Using Lisa-Terminal, a telecommunication software package . . . Lisa functions as . . . an IBM-compatible terminal. When linked to Apple-Net, Apple's newly announced local area network, Lisa makes it possible for users to share peripherals and exchange information and files.

As to the first part of the statement, it is not misleading. Apple did not say that Lisa had *all* the latest technology, but rather, in effect, that Lisa is an innovation. No investor would be misled by this statement, for Lisa was an innovation. If anything, a reasonable investor might be put on notice to the fact that "latest technology" might mean "unproven" or "uncertain" technology.

The second part of the statement is also not misleading, but for a different reason. Plaintiffs have elected to omit key portions of the January 19, 1983 news release which provided full disclosure of the actual state of affairs. The key to plaintiffs' argument is that Lisa was not IBM compatible when it was introduced. But in fact, the press release never made such a promise. The full text around Statement #6 illuminates this fact:

> Using LisaTerminal, a telecommunication software package *being developed* by Apple, Lisa functions as . . . an IBM compatible computer.

Not only did Apple disclose that IBM-compatibility did not yet exist, i.e., it was "being developed," but the company expressly stated that "AppleNet, the Ethernet interface device, and the 3270 data communications package will be available *in late 1983.*" Defendants' Exh. A-2 at 30. In fact, on November 16, 1983, Apple issued the first shipment of both LisaTerminal and the Apple Cluster Controller, products giving Lisa IBM-compatibility as promised.

In their moving papers, defendants admit that AppleNet ultimately was aborted, but aver that the decision to do so was not made until late 1983, after the close of the class period. Furthermore, defendants state that through the summer of 1983 AppleNet was on schedule for a January 1984 release, i.e., only a month behind schedule. Defendants' argument is that because AppleNet was not scheduled to appear on the scene until after the close of the class period, and AppleNet was approximately on schedule throughout the class period and only scrubbed after the class period ended, there was nothing material to disclose during the class period. The logic of this argument is quite appealing.

Plaintiffs do not attempt to attack the IBM-compatibility issue on the basis of what Apple said, but on the basis of what Apple knew. Thus this issue is largely one of

scienter for plaintiffs. They have produced several internal Apple documents showing that Apple management handled the compatibility issue very poorly. *See, e.g.,* Plaintiffs' Exhs. 27, 33, and 86. The truth is that as 1983 progressed, Apple officials became more acutely aware of the need for Lisa to be able to interface with IBM products, as well as their own failure to make provisions to accomplish this feat. Nevertheless, mismanagement is not the issue. The question is whether the investor was misled. Plaintiffs have not provided evidence of any representation to the public made by Apple regarding IBM-compatibility other than the January 19, 1983 press release introducing Lisa. That press release was not misleading, for it made no promise of compatibility before "late 1983." In short, the Court finds that there is no material fact that defendants were obligated to disclose to avoid misleading the public with respect to Statement #6.

STATEMENT #7:

On January 31, 1983, Steven Jobs stated in *Business Week:*

> I don't think we will have any trouble selling all the Lisas we can build.

This is a flat out statement of opinion. Statements of opinion are only actionable under the federal securities laws when they lack a sound historical or factual basis. *See Newbern,* 488 F.2d at 745-46 (9th Cir.1973). As a historical matter, Jobs was speaking from an experience in which he had participated in the development of Apple from an outfit working out of his garage to a company grossing hundreds of millions of dollars in sales. Certainly as a historical fact, Apple had never been unable to sell its product. As a factual matter, internal forecasts at Apple were optimistic about Lisa's prospects and Jobs had ample basis in fact for his statement. Thus, as an expression of opinion, Statement #7 is not actionable.

In connection with Statement #7, it is worth pointing out the context in which the statement was reported. The January 31, 1983 edition of *Business Week* magazine ran a story about Lisa entitled, "Apple takes on its biggest test yet." The opening line of the article sets the tenor for the entire piece and powerfully illustrates the context in which Jobs' statement was publicized. The article begins:

> If the computer industry were a circus, Apple Computer, Inc. would be a high-wire acrobat performing without a net.

Business Week, 1/31/83 at 70.

The article goes on to refer to the fact that Apple was "in the riskiest phase yet of its brief history," and was "going for broke" with the introduction of the Lisa, a product generating "many questions [from] industry observes." Without going into all details, it suffices to say that the article thoroughly canvasses those "many questions" and presents a decidedly sobering picture of Apple's prospects with Lisa. The Court must assume that Statement #7 reached the public via this article since plaintiffs indicate as much with their quotation. Seen in this light, not only is the statement not misleading, but virtually no disclosure by Jobs at that point would have significantly altered the total mix of information already available to investors.

STATEMENTS #8 and #9:

On April 14, 1983, the Wall Street Journal published an article entitled, "Some Warm Up to Apple's Lisa, But Eventual Success Is Uncertain." The article begins by noting the "great confidence at Apple about Lisa. Two quotes are provided and they are Statements #8 and #9 of plaintiffs. The first is the view of Steven Jobs and the second is that of John Couch. The statements were as follows:

> #8 Lisa is going to be phenomenally successful in the first year out of the chute.
>
> #9 This division [that developed Lisa] is going to make Apple's growth before this look small.

Both of these statements fall into the category of expressions of opinion. Due to the predictive nature of these expressions, the Court agrees with plaintiffs that these statements essentially are predictions or forecasts. It does not follow from this characterization that the Court's analysis of materiality should differ with respect to these statements.

Plaintiffs assert that under the court's analysis in *Marx v. Computer Sciences Corporation*, 507 F.2d 485, 490 (9th Cir.1974), because there was a "disparity between the parties in access to the information necessary to judge the accuracy of the forecast, the company had a duty to disclose all pertinent facts relating to the forecast." *Opposition Brief* at 62. This analysis is applicable to the present case, but not in the fashion envisaged by plaintiffs. *Marx* it not a fraud on the market theory case. Indeed, *Marx* predates the Ninth Circuit's acceptance of the fraud on the market theory in *Blackie*. Mr. Marx was a "knowledgeable and experienced private investor" who bought stock in Computer Sciences Corporation ("CSC") in reliance upon a favorable forecast announced in a well-publicized speech delivered by a CSC director and vice president. An explicit premise of the *Marx* court's conclusion that the forecast might create liability was that the parties were at a disparity in terms of their "access to the information necessary to judge the accuracy of the forecast." 507 F.2d at 490.

The fraud on the market theory does not focus on the relative information gap between the parties, but rather on the information gap existing between what is known by the defendant and what is known by the general market. Adapting the *Marx* premise to our case in this light, it is

clear that Apple had a duty to disclose, vis-a-vis Jobs' and Couch's predictions, only if there was a disparity between what was known by Apple and what was known by the market. This is simply another way of asking whether qualifications or disclosures by Jobs and Couch — which would have made their predictions not misleading — would have altered the total mix of information available to the reasonable investor.

One need look no further than the *Wall Street Journal* article of April 18, 1983 (in which Statements #8 and #9 appeared) to see that Apple's optimistic forecast was suitable tempered by other statements reported in the same article. The author of the article informally canvassed the opinions of industry analysts and users presenting a balanced and slightly skeptical view of Apple's prospects for success with Lisa. The article noted various problems with Lisa, including unproven technology ("Lisa's novelty is likely to make buyers wary."), lack of IBM compatibility, questions about software, high price ("Price is a major issue."), and the inclination of buyers to move slowly in gambling on Lisa (The chairman of a market research company stated that "it will be about a year before companies start deciding to make volume purchases."). Seen in the context of an article raising serious doubts about Lisa's prospects for success, the Court is unable to find defendants had a duty to disclose negative facts in order to prevent their predictions in Statements #8 and #9 from being materially misleading.

STATEMENT #10:

Statement #10 is also drawn from the *Wall Street Journal* article of April 13, 1988. The words are those of Apple product marketing manager Barry Smith and the five sentences attributed to Smith are dispersed in two different parts of the article. Taken together these sentences compromise Statement #10 and they are as follows:

> [T]he Company has increased by 50% its estimate of how many machines it should make by the end of the 1984 first half. What we're finding is the reception of Lisa has been very strong.
>
> We find people willing to put down $10,000 without blinking an eye.
>
> [M]ore companies are willing to commit themselves to larger orders than Apple had expected. They're talking larger numbers of their first order, and a quicker reorder.

Unlike the preceding statements, Statement #10 is a compilation of assertions of fact, not opinion. The determination of whether this statement is actionable involves a comparison between the content of the statement and the reality at the time the assertions were made. An examination of Apple internal reports and forecasts for the period preceding the April 14th statement reveals that at least part of Statement #10 is factually correct. Specifically, plaintiffs admit that in March 1983 Apple did increase its projected sales of Lisa by approximately 50% for fiscal year 1983. Furthermore, the backlog of orders for Lisa grew steadily through mid-June of 1983. At the time that Statement #10 was made, Apple had a backlog of orders for Lisa that exceeded 10,000 units. In other words, at a unit price of approximately $10,000, the value of the Lisa order backlog exceeded $100 million in April 1983 — nearly two months before Lisa even had been shipped.

The problem with Statement #10 is that it gives the impression that these "larger orders" are binding commitments to purchase Lisa. A reasonable investor reading Statement #10 would conclude that Apple was actually receiving firm orders for the sale of Lisas. The statement that "[w]e find people willing to put down $10,000 without blinking an eye" strongly suggests that people have put down $10,000 to purchase Lisa. The statement that

"more companies are willing to commit themselves to larger orders" strongly suggests that companies have made a binding commitment to purchase Lisas. In fact, neither suggestion is accurate because the commitments that Apple was referring to were non-binding. As plaintiff's have pointed out, the backlog which was the basis for Statement #10 was "soft," i.e., there was no penalty for cancelling orders. So even if buyers had put down $10,000 to place the order — and it is not clear that any such financial commitment was ever obtained — the fact is that buyers were not irrevocably bound to purchase until the product was ready for shipping.

It is conceivable that investors may have been aware that the commitments referred to in Statement #10 were non-binding, but defendants have not made such an assertion. Accordingly, the Court must assume for the purposes of this motion that this information was not available in the market. Without information alerting one to the fact that the backlog which formed the basis of Apple's supposed commitments was "soft," Statement #10 is misleading. In order to satisfy the standard of Rule 10b-5, Apple had a duty to disclose the fact of the revocability of the commitments in order to negate the misleading effect of Statement #10. Hence the Court finds that Statement #10 may have been a misleading statement of material fact and therefore denies defendants' motion for summary judgment with respect to the materiality of Statement #10.

STATEMENTS ##11-14:

Statements ##11-14 share a common theme in that they reflect Apple's expression of satisfaction at the market's reception of Lisa prior to shipment of the computer. The text of the statements are as follows:

> #11 We are extremely pleased with the market acceptance and orders to date for our Lisa personal office system.

(4/28/83 by defendants Jobs and Markula in Apple's Second Quarter Report to Shareholders)

#12 The acceptance of Lisa among accounts has been very strong. I would say, however, that here has been one small surprise . . . and that is the interest by private individuals at the dealer level in the Lisa. The demand in that channel has exceeded our earlier expectations.

(5/6/83 by Floyd Kvamme, Executive Vice President for Marketing and Sales at Financial Analysts Meeting)

#13 The interest by individuals at the dealer level has surprised us. . . . Major accounts are going about as we had expected but orders are higher than we thought from dealers.

(5/16/83 by Kvamme in *ISO World*, a Framingham, Massachusetts periodical)

#14 Hoar says that the company is quite pleased with the level of orders placed for the Lisa which he says are double what had been anticipated at the release stage.

(6/5/83 by defendant Hoar in *The Providence*, a Providence, Rhode Island periodical)

There are two ways a reasonable investor might assess this information. An investor might take these views of Apple to be expressions of opinion, reinforcing Apple's other optimistic statements concerning Lisa's prospects. To the extent that Statements ##11-14 can be construed to be expressions of opinion they are not actionable because Apple had a "rational" basis for such assertions. *See Marx*, 507 F.2d at 490 n. 7. This rational basis is found in the fact that the optimism about dealer acceptance and orders was reflected in the actual reports and orders received from dealers.

Alternatively, a reasonable investor might view these statements as representations of fact. Insofar as any part of Statements ##11-14 are factual, they are factually correct. As outlined in Apple's papers in support of this motion, Apple's backlog of orders outstripped original expectations through mid-June of 1983. Apple's own internal forecast for fiscal 1983, dated October 1982, pegged Lisa sales for the entire 1983 year at 10,300 units. Yet in early April of 1983, Apple already had outstanding orders for Lisa exceeding 10,000 units. Indeed, plaintiffs admit that as late as mid-June of 1983, Apple had a backlog of Lisa order of nearly 15,000 units. Dealer reaction was particularly favorable and dealer orders alone were forecasted to exceed the overall sales objective for fiscal 1983. The article in which Statement #13 appeared included reference to the periodical's own survey which corroborated the remarks of Apple's Kvamme. To wit, *ISO World* was told by dealers whom it contacted that the "response has been very favorable, much greater than expectations." Plaintiff's Exh. 4. The president of a computer outlet in San Jose, California reported that "[w]e have on order more Lisas than any other machine we have sold, including the Appel II and the IBM PC." *Id.* Thus, as a matter of objective fact, the content of Statements ##11-14 is accurate and is not actionable under the securities laws.

STATEMENT #15:

Statement #15 is a five sentence blurb that appeared June 13, 1983, in a Reuter wire service financial report. The statement quoted an Apple official named DeVaughn as representing that:

> Apple began volume shipments June One [1983] of its new $10,000 Lisa Computer. "The product has been well-received and shipments are running ahead of expectations."

This is a difficult statement to assess for several reasons. First, DeVaughn is never identified in the news blurb and plaintiffs have not identified DeVaughn in their papers, instead referring to him simply as an "Apple spokesman." Second, the context of the statement is not given. When did DeVaughn say this and what else did he say? Finally, to whom did DeVaughn make the statement? Was it a press release or an interview? If it was a press release, were his remarks reported in full elsewhere? Due to the fact that in this motion the Court must view all facts and make all factual inferences in the light most favorable to the plaintiff, the Court will assume that the statement was made by an Apple official to the general public and that no other qualifying or explanatory representations accompanied the statement.

Even while ignoring these unresolved questions, the Court finds that Statement #15 is not actionable. Apple did begin volume shipments of Lisa in June of 1983. Internal Apple documents reflect that Apple actually shipped and sold 1,432 Lisas in June 1983. Defendants' Exh. A-6 at 15102400. With respect to the assertion that shipments were running ahead of expectations, the question is less clear cut. Apple refused to publicize what those expectations were. Part of the Reuters blurb that was not quoted by plaintiffs stated: "DeVaughn declined to give any specific estimates on total third quarter sales and profits or shipment figures for the Lisa computer." Thus the only expectations implicated by Statement #15 are those of Apple itself.

In surveying the documents, the Court is unable to pinpoint precisely what Apple's productions expectations were at the beginning of June 1983. It is clear that those expectations must have changed in view of Apple's failure to meet its own internal (and secret) goal of initiating shipments in late spring. In a June 7, 1983 "Corporate Forecast Report," production for the fourth quarter of

1983 was described as "constrained based on the manufacturing capacity as of June 1st." Defendants' Exh. 14. A report delivered to the Board of Directors on June 27, 1983, stated that approximately 2,000 units would be shipped in the month of June. Defendants' Exh. 43. And an inter-office memo of June 20, 1983 reported that the manufacturing constraint for Lisa in June was 1,900 units and estimated that 1,500 units would be shipped. Plaintiffs' Exh. 43. Taken together, the foregoing figures suggest that Apple expected to ship roughly 2,000 Lisas in June of 1983. When the dust settled, Apple had shipped only 1,430. Based on these figures alone, the Court is not prepared to conclude that Statement #15 was or was not misleading per se. The question then is whether plaintiffs have adduced any evidence to suggest that at the time the statement was made shipments in fact were not running ahead of expectations.

Plaintiffs have failed to state specifically how Statement #15 was a misstatement or misleading. In order to do so, plaintiffs must offer some benchmark of Apple's expectations and then show that at the time the statement was made shipments did not meet these expectations. No such proof has been offered. The only time plaintiffs broach this subject, they do not focus on June shipments, but rather shipments in July. According to plaintiffs, Apple planned to ship less than 700 Lisas in July of 1983. *Opposition Brief* at 34. Yet the defendants have stated in their moving papers, without rebuttal by plaintiffs, that July shipments of Lisa were 1,814 units, a figure over double the estimation offered by plaintiffs. Moreover, combining the figures for the units shipped in June and July of 1983 yields a total figure for shipped Lisas that exceeds 20% of the highest estimated backlog figure. This would seem to indicate that expectations were being met.

The Court has wrestled long and hard over Statement #15 in assessing its materiality. After examining the

voluminous record more than once in search of an answer, the Court is unable to find any evidence that at the time Statement #15 was made it was a material misstatement or misrepresentation. Furthermore, the Court finds that plaintiffs have not come forward to produce any evidence to that effect. The words of the Supreme Court in the recent *Celotex* case seem particularly appropriate here:

> The moving party [in a motion for summary judgment] is "entitled to judgment as a matter of law" [when] the nonmoving party has failed to make a sufficient showing on an essential element of her case with respect to which she has the [ultimate] burden of proof.

106 S.Ct. at 2553.

Because plaintiffs have not adduced evidence showing that Statement #15 was a misstatement or misrepresentation of material fact, the Court will grant summary judgment to defendants on the issue of the materiality of Statement #15.

STATEMENT #16:

The final statement identified by plaintiffs as the basis for this class action suit is a representation made by defendants Jobs and Sculley in Apple's Third Quarter Report to Shareholders, dated July 27, 1983:

> Customer shipments of the Lisa system began on schedule and we remain pleased with its market acceptance, order rate and dealer enthusiasm. Lisa is clearly being recognized as an important force in the office market.

This statement can be broken down into three parts — fact, opinion, and puffing. The factual component is the assertion that Lisa shipments began on schedule. As already noted, this is factually correct. The opinion component is that Apple itself remained pleased with Lisa general market acceptance. This expression of opinion is

only actionable if it does not represent management's view, lacks a rational basis, or is insincere. The question of sincerity is better left to the upcoming discussion of scienter. As to the other factors, it is clear that this statement did represent management's view. Indeed, it was made by the two top management officials to the shareholders on behalf of the management of Apple.

The remaining question is whether there was a rational basis for Statement #16. Although plaintiffs offer several arguments to show that Apple had no rational basis for its optimism in late July of 1983, none of their contentions are convincing. To begin with, plaintiffs argue that the Lisa backlog was decreasing by July indicating poor reception of the product by the public. It is true that the backlog of nearly 15,000 units was estimated at 11,000 units in the report to the board of directors on June 27, 1983. But a closer look at this estimate reveals that plaintiffs' interpretation is fallacious. In fact, the report of June 27, 1983, states at the outset that "demand [is] good" for Lisa and that the "backlog [is] conservatively stated at 11,000 units." Defendants' Exh. 43. The report goes on to state that "Beta test results at 17 companies were positive" and that "[a]lmost all Beta sites will buy their units." *Id.* Taken as a whole, this report presents a very positive viewpoint on Lisa's acceptance by the public. If there was some slippage in backlog, it could have been explained in part by the fact that over 1,000 units were shipped in June to meet the backlog. Moreover, Apple was aware that the backlog was "soft" and a slight dip would not be a matter of major concern. Taking all these factors into consideration, there was more than a rational basis for satisfaction with Lisa's acceptance as of June 27, 1983.

Plaintiffs next suggest that reports from Apple's Dealer Advisory Council at its July 12-13, 1983 meeting suggest that there was no basis for an optimistic assess-

ment of Lisa's market reception. If one looks at the condensed minutes of the meeting, it is clear that plaintiffs are mistaken. For although the minutes do state that "the backlog of orders is decreasing," Plaintiffs' Exh. 76, the opening line of the remarks on Lisa states that "[i]t appears that product appeal is more widespread than expected." The minutes also state that "[c]orporate sales are slower than expected, possibly because of the longer evaluation and/or buy cycle and because of the growing strength of IBM." *Id.* Ultimately, the dealer suggested that Apple "relaunch" Lisa with a beefed up advertising campaign emphasizing "Lisa's uniqueness" and the fact that "Lisa will do things that no other PC [personal computer] can do." Once again, when taken as a whole this report on Lisa's reception is positive and optimistic about Lisa's market acceptance, thus suggesting a rational basis for Statement #16.

The strongest argument that plaintiffs have with respect to the lack of rational support for Apple's publicized optimism in July 1983 is a memorandum of August 15, 1983, which reports that "[o]ur Lisa backlog is now depleted in [the] domestic market." Plaintiffs' Exhibit 81. Assuming that "depleted" means that the Lisa backlog had disappeared, one must infer that the bottom fell out of the Lisa market, for only six weeks before the backlog was pegged at 11,000 units — conservatively. Even more startling is the fact that Apple's own internal July/August 1983 forecast, dated August 1, 1983, predicted fourth quarter sales of 10,000 Lisas and total sales for fiscal 1983 in excess of Apple's 1983 business plan. This contradiction indicates that Apple had a serious problem with the accuracy of its assessment of the Lisa backlog, but it does not establish a dispute, as plaintiffs must in order to prevail here, as to whether Apple's optimism lacked a rational basis. Most importantly, plaintiffs have not demonstrated that as of July 27, 1983, Apple had no rational basis to be pleased with Lisa's

market and dealer reception. On the contrary, the facts suggest that given the evidence available to it — including its own internal forecasts and dealer input — Apple had a rational basis for its optimism.

The final component of Statement #16 is an element of puffing. The statement that "Lisa is clearly being recognized as an important force in the office market" is such an emphatic statement of opinion that it rises to the level of puffery. Lisa was being recognized as an important force in the office market from the moment the computer was introduced in January 1983. Even in light of Lisa's failure, it is still fair to say that Lisa was "an important force" in office computers, if for no other reason than the potential it possessed and the market waves it created. Moreover, boasting such as this is common business practice. Any manufacturer or service provider with any pride in its product would say that its product is an important force or a significant achievement in one field or another. *See, e.g., Zerman v. Ball*, 735 F.2d 15, 20-21 (2d Cir.1984) (finding that an advertising slogan boasting of the recognized significance of broker's advice is not actionable). In short, a reasonable investor reading this boastful part of Statement #16 would not be mislead even if he believed that Lisa was an important force in the office market. And, in fact, a reasonable investor would take whatever facts could be gleaned from the statement and assess it against the published literature describing the market's actual perceptions about Lisa as found, for example, in *The Wall Street Journal* or *Business Week*.

(F) *Summary of the Analysis of Materiality:*

The crux of plaintiffs' argument is that defendants violated the securities laws by making optimistic statements about Lisa and Lisa's prospective success when in fact Lisa faced serious technical and marketing problems. The theoretical underpinning for their argument is the ruling in *Marx v. Computer Sciences Corporation*, 507 F.2d

485, 490 (9th Cir.1974), in which the court found that a jury may find that a defendant, "by ignoring facts seriously undermining the accuracy of [its] forecast, failed to meet the duty imposed by §10(b)." Without modification, this theory simply does not wash in a fraud on the market case. Instead, in a case such as this, a plaintiff must demonstrate materiality by showing that information withheld by the defendant was necessary to make the representation not misleading and that the information, had it been disclosed, would have altered the total mix of information available to the reasonable investor. With respect to all but two of the sixteen statements offered by plaintiffs as proof of material misstatements by defendants, the Court has found that plaintiffs have not demonstrated materiality — either because the statement itself was not misleading or because the information to make the statement not misleading was already available to the market. In light of these findings, the Court concludes that plaintiffs have failed to sustain their burden, in this motion for summary judgment, of coming forward with such evidence that a reasonable jury could find in their favor on the issue of materiality. Good cause appearing therefor, defendants' motion for summary judgment on the issue of materiality is granted with respect to all statements except Statement #5 and Statement #10.

IV. SCIENTER

(A) *Legal Standards:*

In addition to establishing the materiality of a misstatement or omission, to prevail under § 10(b) and Rule 10b-5 a plaintiff must prove that the defendant acted with "some element of scienter." *Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 201, 96 S.Ct. 1375, 1385, 47 L.Ed.2d 668 (1976). Scienter requires a showing of some degree of knowing or intentional conduct done with the intent to deceive or defraud. *Id.* at 193, 96 S.Ct. at 1381. In addition, although the question was reserved by the Court

in *Hochfelder,* the Ninth Circuit has found that reckless conduct may satisfy the scienter requirement of § 10 and Rule 10b-5. *Nelson v. Serwold,* 576 F.2d 1332, 1337 (9th Cir.1978), *cert. denied,* 439 U.S. 970, 99 S.Ct. 464, 58 L.Ed.2d 431 (1978); *Burgess v. Premier Corp.,* 727 F.2d 826, 832 (9th Cir.1984); *Harris v. Union Elec. Co.,* 787 F.2d 355, 369 (8th Cir.1986), *cert. denied,* ____ U.S. ____, 107 S.Ct. 94, 93 L.Ed.2d 45 (noting that Ninth Circuit's position is shared as the prevailing view among the circuits). In elaborating on the concept of "recklessness" in the securities fraud context, this circuit has found that "recklessness" is closer to "a lesser form of intent" than "merely a greater degree of ordinary negligence." *Vucinich v. Paine, Webber, Jackson & Curtis, Inc.,* 739 F.2d 1434 (9th Cir.1984), *quoting Pegasus Fund Inc., v. Laraneta,* 617 F.2d 1335, 1341 (9th Cir. 1980).

Scienter may be established by a showing that the defendants lacked a good faith belief in the accuracy or completeness of their representations. *See Hochfelder,* 425 U.S. at 206, 96 S.Ct. at 1387. In *Hochfelder,* the Court found the intent of Congress to be quite clear that no one may be made liable under Rule 10b-5 and § 10 "unless he acted other than in good faith." *Id.* In addition, in this circuit, the burden of showing scienter may be met in a case of recklessness by showing that the defendants "had reasonable grounds to believe material facts existed that were misstated or omitted, but nonetheless failed to obtain and disclose such facts although they could have done so without extraordinary effort." *Burgess v. Premier Corp.,* 727 F.2d 826, 832 (9th Cir.1984), *quoting Keirnan v. Homeland, Inc.,* 611 F.2d 785, 788 (9th Cir.1980); *see also Bell v. Cameron Meadows Land Co.,* 669 F.2d 1278, 1283 (9th Cir.1982).

Generally speaking, scienter is not an issue suitable for determination in a motion for summary judgment. The rule in this circuit is that summary judgment will not be

granted on the issue of scienter unless "no reasonable inference supports the adverse party's claim." *Vucinich,* 739 F.2d at 1436 (9th Cir.1984).

(B) *General Allegations:*

Consistent with the relevant legal standards, plaintiffs seek to show scienter by showing that defendants either knew the misleading nature of their statements, or made the statements in reckless disregard of adverse facts that could have been disclosed without extraordinary effort.

Plaintiffs have submitted several pieces of evidence suggesting that Apple in general, and Lisa specifically, might face rough seas in 1983. As an example, plaintiffs refer to a memorandum prepared by Trip Hawkins dated April 28, 1982, and directed to the "Executive Staff and Marketing Council." Plaintiffs quote a portion of the memo which warns that "[W]e are currently betting most of our 1983-1984 growth on risky new products." *See Opposition Brief* at 25. Hawkins states that both Lisa and MacIntosh computers have suffered "huge schedule delays" and "harbor great technical risks," yet "both are expected to arrive on time in 1983 and provide dramatic revenue increases for Apple." Hawkins concludes by stating that "we simply can't expect significant sales from these products in fiscal 1983."

Hawkins' memorandum does not conclude on this negative note, however, for he goes on to suggest various "response[s]" to these issues which will allow Apple to confront these challenges. For example, Hawkins argues that Apple's objective should be to "[e]stablish Lisa/Mac-class products as the new standard for competition in the 1980's and secure an installed base lead analagous to that which Apple II currently enjoys," Plaintiffs' Exh. 10 at 533. This refers to the concept of fixing one's computer as a desirable target for third-party suppliers. Hawkins indicates that Lisa might serve as the base for such a strategy which Apple could then exploit by

producing an Apple software development program. The overall tenor of Hawkins' memo is one of constructive criticism. Taken as a whole, it does not support an inference that Apple executive knew Lisa was going to fail or that Apple itself was in trouble.

The facts are clear that Apple and the defendants in this action were fully aware of the risks and challenges they faced. Moreover, Apple officials were prepared candidly to admit that their industry is subject to vicissitudes. An example of such an admission is found within the text of the 1982 Annual Report. While plaintiffs sought to attach liability to part of the statement of director Arthur Rock, they omit reference to the following statement:

> [It is a] mistake to place any kind of [limitation?] on this industry — it's open ended. In terms of the overall computer industry from the time that the first computer was developed 30 odd years ago, anybody who attempted to project computer needs and applications was usually quite wrong. We're still a brand new industry.

(C) *Apple's Internal Forecast:*

The foregoing statement is particularly relevant to plaintiffs' assertions of scienter in connection with Apple's internal forecasts. Before addressing those contentions, some background is necessary. In their brief in support of this motion, defendants provide a detailed description of the forecast process. *See Moving Brief* at 18 n. 9. Plaintiffs have not challenged the accuracy of defendants' description; hence, for the purposes of this motion, the Court will accept Apple's own description of its internal forecast preparation process.

Apple's internal forecast, officially dubbed the "Corporate Forecast Report," was the management's basic predictive tool and was distributed monthly to the executive

staff, general managers, and all members of the Board of Directors. Apple describes its forecast technique as a "bottom up" process, whereby it collected forecasts from dealers and direct sales people in Apple's sales division. Each month, the distribution division and products division, respectively, would collect competitive information and make their own forecasts. These two divisions would then meet with the sales division and the manufacturing and finance divisions at a monthly corporate forecast meeting. At this major monthly meeting, representatives from each of the divisions discussed their respective forecasts and important competitive information, and together the divisions would reach a concensus on a twelve month market demand forecast. Following the fixing of the forecast, the manufacturing division would produce its manufacturing response (hereafter "build plan") in which it reported the number of units it could build in order to meet the market demand forecast. Completing this planning cycle, personnel and raw material purchasing plans were made on the basis of the build forecasts in the build plan.

The obvious purpose of the internal forecast was to provide Apple management with a realistic idea of market demand. Without such an estimate, management would not be unable to make intelligent decisions regarding marketing, procurement of resources, production, or distribution. Apple had a vested interest in insuring the highest degree of reliability for its internal forecasts. Apple not only would derive no benefit, but would risk irreparable injury by generating falsified or deliberately exaggerated market predictions. Moreover, for competitive as well as practical reasons, Apple maintained the forecasts as confidential information. Plaintiffs have never alleged that the forecasts themselves were ever made public or used for any purpose other than as a

crucial guide to Apple's own internal management process.

(D) *The Dispute Over Scienter:*

Some of defendants' most creative argumentation is dedicated to establishing the non-existence of sufficient evidence of scienter to withstand the present motion. The key component of defendants' argument is to miscast plaintiffs' position and thereafter to annihilate the strawman. To wit, defendants reduce plaintiffs' scienter argument to the simple asertion that "Apple made and stated the wrong judgments about Lisa's risks and prospects for success" *Reply Brief* at 8. Further, Apple argues that plaintiffs' position is grounded:

> [O]n the proposition that when a corporation in good faith reaches a conclusion or opinion on a matter of subjective judgment concerning success and risk and states its conclusion publicly, it nevertheless has a federal securities law disclosure obligation to judge its opinion and conclusion to be wrong, and to state the "correct" conclusion, or not to make the statement actually made.

Reply Brief at 14.

In fact, this is a significant oversimplification of plaintiffs' position. The point is not that Apple made erroneous business judgments, but rather that Apple officials made positive statements to the public about Lisa even while knowing certain negative facts about the new computer and its prospects for success. Defendants moved out from behind the generous shield of the business judgment rule once they started to make public statements about Lisa. At that point, the federal securities laws came into play and defendants were liable to the same extent as any other business actors for the content of their statements. There is nothing revolutionary about this. Nor is there anything calamitous in the proposition — which is the

accurate discription of plaintiffs' position — that once defendants spoke publicly they had a duty to avoid misleading the public. This did not require Apple officials to view their statements as wrong, but merely to be careful *not* to be wrong or misleading. In the context of the issue of scienter, the implication for a defendant who misleads or misstates is that he may be held liable if the plaintiff can show that the defendant knew or was aware of facts which suggested the error of his statement.

(E) *Analysis and Conclusion of the Scienter Issue:*

For purposes of analyzing scienter, the Court begins from the premise that both Statements #5 and #10 were material. The question then is whether defendants knew, were aware of, or were recklessly indifferent to facts that contradicted their statements and thereby put them on notice as to the misleading character of Statements #5 and #10. As described in the discussion of materiality, Statement #5 was made in a context in which Apple officials were aware of serious problems with the Twiggy disk drive. At the very least, Apple had reasonable grounds to believe that material facts were being misstated, "but nonetheless failed to obtain and disclose such facts although they could have done so without extraordinary effort." *Burgess v. Premier Corp.*, 727 F.2d 826, 832 (9th Cir.1984), *quoting Kirnan v. Homeland, Inc.*, 611 F.2d 785, 788 (9th Cir.1980). Similarly, with respect to Statement #10, Apple officials were aware of the "softness" of their backlog. Given the non-binding quality of the orders for Lisa and the evidence on the record establishing knowledge of the hazards of relying on backlog estimates, plaintiffs have demonstrated sufficient facts to withstand defendants' motion on the issue of scienter with respect to Statement #10. Therefore, the Court will deny defendants' motion for summary judgment on this issue of scienter with respect to Statements #5 and #10.

V. CONCLUSION

The Court has found that the vast majority of the challenged statements made by defendants were either not misleading or were stated in a context which did not create a duty of disclosure on the part of defendants. Adhering to the language and spirit of the Supreme Court in *TSC*, this Court has attempted to make the "delicate assessments" necessary to ascertain the materiality of these statements to an investor, given the analytical context of a fraud on the market theory of recovery. In light of *TSC* and the many Ninth Circuit cases applying *TSC*'s teachings, the Court therefore HEREBY GRANTS DEFENDANTS' MOTION FOR SUMMARY JUDGMENT ON THE ISSUE OF MATERIALITY WITH RESPECT TO ALL OF PLAINTIFFS' CASE EXCEPT STATEMENTS #5 and #10.

On the issue of scienter, the Court has found it necessary to assess only Statements #5 and #10. Plaintiffs have raised facts and inferences that are subject to dispute with respect to these two statements. Accordingly, the Court must and HEREBY DOES DENY DEFENDANTS' MOTION FOR SUMMARY JUDGMENT ON THE ISSUE OF SCIENTER.

IT IS SO ORDERED.

APPENDIX
C

[696 F.Supp. 490]

In re APPLE COMPUTER SECURITIES LITIGATION.

Master File No. C-84-20148(A)-RPA.

United States District Court,
N.D. California,
San Jose Division

July 31, 1987.

AGUILAR, District Judge.

On April 30, 1987, the Court issued an "Order Granting in Large Part Defendants' Motion for Summary Judgment" (hereafter the "Order"). Plaintiffs now move for partial reconsideration of the Order. In addition, plaintiffs have brought their own motion for partial summary judgment. Defendants have opposed both motions in a single brief, and a series of additional submissions, which in turn were opposed by a series of submissions by plaintiffs. The papers have now settled. The Court has deemed the matter submitted without the favor of oral argument. Having received and read all the papers submitted, and having reread and reconsidered its earlier Order, the Court finds and orders as follows.

(A) *Statement ##8 and 9:*

Plaintiffs have expended a great deal of time and energy asserting that these Statements are material. These efforts have not altered the Court's conclusion, but they have served to provide the Court with an opportunity to amplify its ruling.

In analyzing Statements ##8 and 9, the Court agreed with plaintiffs' characterization of these Statements as predictions or forecasts. The Court then went on to state that "[i]t does not follow from this characterization that the Court's analysis of materiality should differ with respect to these statements." *Order* at 25. In fact, once

having categorized the Statements as opinions or forecasts, the Court should have analyzed them, at least at the initial level of analysis, differently than statements of objective fact. *See, e.g., Marx v. Computer Sciences Corporation,* 507 F.2d 485, 490 n. 7 (9th Cir.1974); *G & M, Inc. v. Newbern,* 488 F.2d 742, 745-46 (9th Cir. 1973).

In this case, Statements ##8 and 9 are expressions of opinion. As such, the standard in this circuit regarding their materiality is whether the Statements were sound and justified. In the words of the court in *Marx,* were the Statements "reached in a rational fashion." 507 F.2d at 490 n. 7. As explained in several places in the Order (see in particular the discussion of Statements ##11-14), defendants had a rational basis for their optimism, grounded in both historical and contemporary fact. This rational basis is sufficient to immunize defendants from liability for Statements ##8 and 9.

Having made that analytical digression, the Court affirms its earlier treatment of Statements ##8 and 9 in the Order. Even if the Statements are assessed as representations of objective fact, they are not materially misleading. Plaintiffs' argument is that these Statements were misleading and that defendants had a duty to disclose negative information in order to avoid misleading the public. The Court concluded that the article in which the Statements were reproduced itself contained exactly the type of negative information plaintiffs' would find necessarily disclosed in order to avoid misleading market investors. Contrary to plaintiffs' exaggerated assertions, the Court did not find it sufficient that "someone somewhere" express an opinion contrary to management's public statements. *Memorandum in Support of Plaintiffs' Motion for Reconsideration of Order Partially Granting Defendants' Motions for Summary Judgment* (hereafter "Moving Brief") at 9. Instead, the Court found that the duty of disclosure is met when negative statements, made

in the context of a skeptical news article, are juxtaposed to and essentially bracket misleading representations appearing in the same article. Upon reconsideration, the Court affirms this conclusion, adding as additional support the above discussion treating the Statements as expressions of opinion. Summary judgment on behalf of defendants was proper with respect to Statements ##8 and 9.

(B) *Statements ##11-14:*

Plaintiffs raise several point vis-a-vis Statements ##11-14. The Court finds that although artfully asserted, none of these points warrants a reversal of the Court's Order. First, plaintiffs contend that Statements ##11, 13, and 14 convey the impression of firm orders as opposed to the reality of "soft," non-binding commitments. Plaintiffs contend that a "reasonable investor could read those statements as implying firm orders." *Moving Brief* at 26. This goes too far. In each of these Statements, Apple represents that *it* is pleased with the public's response to Lisa. This is expressed in general terms, without reference to qualitative yardsticks. Indeed, the yardstick invoked is *Apple's* expectations. As a matter of objective fact, these were accurate Statements at the time they were made. Thus, liability does not attach.

By way of comparison, the Court found that Statement #10 was misleading because it was an affirmative representation that money had changed hands in ordering Lisa. As noted by plaintiffs, the Court found that a reasonable investor "*would*" conclude that Apple was actually receiving firm orders for the sale of Lisas. There is a significant difference between the Court's conclusion as to what a reasonable investor "would conclude" in reference to Statement #10, and plaintiffs' argument of what a reasonable investor "could read . . . [Statements

11, 13, and 14] as implying." The difference is that the former is actionable and the latter is not.

Plaintiffs also take issue with the Court's treatment of Statement #12, contending that it was deceptive. Plaintiffs support this argument largely by reference to documents and information generated after Statement #12 was made. This is hardly fair play. The Court will stand by its ruling with respect to Statement #12 as well as Statements ##11,13, and 14.

(C) *Statement #15:*

The Court has reexamined Statement #15 in light of the parties' further briefing. The Order put plaintiffs on notice to the fact that they had not adequately described the context of the publication of Statement #15. Due to the fact that the issue of publication was not contested, the Court gave plaintiffs the benefit of the doubt.

Defendants now expressly question whether Statement #15 was published in such a way as to have the potential to affect the price of Apple stock. Defendants commissioned an investigation into various business news sources to locate any possible reporting of Statement #15. The investigation proved fruitless, suggesting that the Statement was not published in any source other than the one identified by plaintiffs. However, defendants do not challenge the allegation that the Statement was published in the Reuter Financial Report of June 13, 1983. Absent contrary evidence, the Court must assume that the Statement was published on June 13, 1983 in the Reuter Financial Report. The question then is whether such publication could have affected the market price of the stock.

The declaration of John Torkelsen indicates that such publication would be reflected in the price of Apple stock. The Court finds this to be rather weak evidence, but it is

sufficient to make a prima facie case of effect on the price of Apple stock.

There still remains the question of the materiality of Statement #15. The Court has reconsidered its position in light of the additional briefing and now finds that the materiality of Statement #15 is properly left to a jury to decide. In its earlier analysis, the Court focused on the content of the Statement, and in particular, the aspect of the Statement relating to Apple's expectations. The Court continues to find this analysis appropriate. What the Court failed to address adequately was the issue of timing. When the Statement was made, no shipments had been made. Had the Statement been made two weeks later, the issue of materiality would take on a different complexion. But given the timing of the Statement, a jury could reasonably find that the Statement was material. Accordingly, the Court reverses its position and now finds that Statement #15 is not properly disposed of at summary judgment. Defendants' motion for summary judgment with respect to Statement #15 is therefore denied.

(D) *Statement 16:*

Plaintiffs seek reconsideration of the Court's ruling on this Statement on several grounds. The Court rejects plaintiffs' analysis and affirms its earlier ruling. There was a rational basis for Statement #16 and it was not a material misstatement or misrepresentation of fact. The only item raised by plaintiffs upon which the Court wishes to comment is the reference to the proper legal standard for ruling on motions for summary judgment. Plaintiffs object to the Court's use of the word "establish." Contrary to their expressed view, plaintiffs did have the burden of raising some material issue of fact. Defendants came forward with evidence suggesting a rational basis for their Statement. At that point, plaintiff had the burden of establishing some material fact tending to show that Apple's optimism lacked a rational basis. Plaintiffs

were unable to do so. Consequently, summary judgment was appropriate.

(E) *Additional Statements:*

Plaintiffs allege that two additional statements are actionable. These two statements will be denoted Statements ##17 and 18 and are as follows:

Statement #17:

> [I]n our own experience, price has not been an issue, even with Lisa. . . .
>
> . . . We announced at NCC the Applenet, our local area network concept, which will be shipped in early 1984.

Defendant John Sculley remarks to group of Financial Analysts on August 12, 1983.

Statement #18:

> Are Sales of Lisa Dropping off? Are they below projection? What major sales can be used as examples of Lisa's acceptance?
>
> We continue to be satisfied with the sales of Lisa which, as you know, began shipment in late June. Lisa is meeting our Fiscal Year 83 projections, so we're right on target with sales.

Questions and Answers Drafted for Executive Briefing Tour, September 12-16, 1983.

To the Court's knowledge, Statement #17 was not raised in plaintiffs' papers in opposing the motion for summary judgment. Nevertheless, in the spirit of fairness, the Court will now consider the matter.

The first part of Statement #17 is clearly not actionable. Even excerpted in part and out of context, the Statement about Lisa's price is neither material nor a misstatement. When properly put in context, there is no doubt that it is non-actionable. Similarly, the second part of Statement #17 regarding Applenet is non-actionable.

The topic of Applenet and IBM compatability was discussed in the Order within the discussion regarding Statement #6. The sole item offered by plaintiffs contradicting Statement #17 is an interoffice memo dated contemporaneously with Sculley's public statement. No reasonable jury could find, in light of all the evidence about Applenet, that this memo raises a triable issue of fact with respect to Sculley's remarks. Accordingly, the Court hereby grants defendants' motion for summary judgment with regard to Statement #17.

To matter how vigorously plaintiffs stab at the strawman erected in Statement #18, their efforts are to no avail. As defendants point out, plaintiffs have adduced no evidence showing that Statement #18 was ever released to the public. Without public disclosure, Statement #18 cannot be said to have contributed to an improper inflation in the price of Apple stock. Therefore, the Court hereby grants defendants' motion for summary judgment with respect to Statement #18.

(F) *The Question of Timing and the Duty to Disclose:*

In their *Moving Brief* in this motion for reconsideration, plaintiffs raise an argument about timing and defendants' duty to disclose. The gist of the argument is that defendants had a continuing duty to monitor the accuracy of past statements. For example, once Apple learned that the Lisa order backlog had been depleted, the company was obligated to publicly correct earlier statements to the effect that the product was being well received. Plaintiffs dub this responsibility, "a duty to correct." *Moving Brief* at 19. This is a new argument raised for the first time (as far as the Court can discern) in this motion for reconsideration.

Plaintiffs have set the time frame for this duty to correct as beginning at least by August 15, 1983. The parties agree that disclosure was made on September 23, 1983. Basically, then, the argument breaks down to a

thirty-nine day period in which defendants allegedly knew that some of their prior statements were false or misleading, yet did not step forward to correct a continuing public misperception.

The first task is to identify those Statements which are alleged to have become misleading or false. Plaintiffs have engaged in general accusations rather than specific references, but given the scope of the case this is understandable. Having surveyed the list of Statements yet again, the Court finds that Statements ##8 and 9 are the only Statements potentially raising a duty to correct. However, the Court's analysis in the Order vis-a-vis the misleading character of Statements ##8 and 9 is equally applicable here. Whatever potential to mislead these Statements possessed was countered in the same article in which the Statements appeared. If the Statements themselves can be said to have had lingering effects in terms of continued reliance by investors, so too did the contrary information published in the same article. In short, the Court concludes that defendants did not breach any "duty to correct."

(G) *Plaintiff's Motion for Partial Summary Judgment;*

The Court agrees with defendants' characterization of this motion as another angle on the motion for reconsideration. The Court has made its rulings on materiality in this order and the earlier Order, and will not render an advisory opinion on what was or was not material in this case as of August 15, 1983. Accordingly, plaintiffs' motion for partial summary judgment is HEREBY DENIED.

(H) *Dismissal of the Outside Directors:*

Now that the dust has settled, it is time to turn to the issue of the liability of the outside directors. The three remaining Statements which form the basis of plaintiffs' case are not sufficient to state a claim against the four outside directors. A party "must have a duty to disclose

information before his failure to do so will support liability." *S.E.C. v. Rogers,* 790 F.2d 1450, 1459 (9th Cir.1986), *citing Strong v. France,* 474 F.2d 747, 752 (9th Cir.1973). A directorship in itself does not impose a duty to insure that all material adverse information about Lisa was conveyed to prospective purchasers of Apple stock. *Decker v. Massey-Ferguson, Ltd.,* 681 F.2d 111, 119 (2d Cir.1982); *Lanza v. Drexel,* 479 F.2d 1277, 1289 (2d Cir.1973) (en banc).

In this case, the three Statements in question cannot be attributed to the outside directors. The Statements were not part of quarterly reports or any other official Board of Director publications. Plaintiffs have not connected these three Statements with any of the outside directors, nor have they demonstrated that the outsiders had any duty to disclose with respect to these Statements. Furthermore, there is no controlling person liability, *see Burgess v. Premier Corp.,* 727 F.2d 826, 832 (9th Cir.1984), nor is there any liability for aiding and abetting. *See Orloff v. Allman,* 819 F.2d 904 (9th Cir.1987); *see also Harmsen v. Smith,* 693 F.2d 932 (9th Cir.1982), *cert. denied,* 464 U.S. 822, 104 S.Ct. 89, 78 L.Ed.2d 97 (1983). Good cause appearing therefore, the outside directors' motion for summary judgment is HEREBY GRANTED.

(I) *Summary:*

The Court has struggled mightily to provide plaintiffs with a fair opportunity to respond to defendants' motions. Despite submitting literally thousands of pages of briefs and exhibits, plaintiffs have not, for the most part, succeeded in showing that they have a viable case. The fact that most of the directors of a corporation sold a small fraction of their stock in that corporation during a volatile period in the life of the relevant industry does not, in itself, state a cause of action for violation of the securities laws. Nor do general statements of optimism — in this case without reference to specific sales predictions or

profit projections — create liability for securities fraud. The Court has gone the extra mile with plaintiffs and has not yet arrived at the case that has been advertised at oral argument or in flowing introductions to briefs. Therefore, with the exception of the revival of Statement #15, plaintiffs' motion for reconsideration of the Court's Order of April 30, 1987 is HEREBY DENIED. Plaintiffs' motion for partial summary judgment is also denied.

IT IS SO ORDERED.

APPENDIX

D

[690 F.Supp. 872]

IN RE APPLE COMPUTER SECURITIES LITIGATION.

Master File No. C 84-20148(A) RPA.
United States District Court, N.D. California.
Dec. 14, 1987.
As Corrected Dec. 18, 1987.

ORDER GRANTING SUMMARY JUDGMENT AND DENYING MOTION TO AMEND COMPLAINT

AGUILAR, District Judge.

I. INTRODUCTION.

After a hiatus of several months digesting the Court's order denying plaintiffs' motion for reconsideration, defendants' have brought a motion for summary judgment against the three remaining actionable statements made by Apple officials. The basis for the motion, *inter alia,* is that defendants' lacked scienter within the meaning of the securities laws. Not to be left motionless, plaintiffs have filed a countermotion to amend the complaint. Plaintiffs seek to add three California causes of action to their complaint which would exactly track the federal § 10(b) and Rule 10b-5 claims. As explained below, the Court will grant the motion for summary judgment and thereby moot plaintiffs' motion to amend.

II. FACTS.

The facts of this case have been detailed in a previous ruling of this Court. *See, e.g., Order Granting In Large Part Defendants' Motion for Summary Judgment* (April 30, 1987) (hereafter the "Order"). The net effect of the Order and the Court's subsequent ruling in response to a motion for reconsideration[1] was that the Court rejected

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[1]The order in response to the motion for reconsideration was filed on July 31, 1987. The order was untitled and hereafter will be referred to as the "Reconsideration Order."

15 of the 18 statements which formed the basis of plaintiffs' case. The three remaining statements are Statements ##5, 10, and 15. The Court did not dismiss these statements because on the record before it, and construing all facts and inferences from facts in the light most favorable to plaintiffs the non-moving parties, there were questions of material fact remaining.

Defendants now move for summary judgment on the three remaining statements arguing that plaintiffs have not put forth evidence raising a triable issue of material fact with respect to scienter. They also indirectly raise the issue of materiality again. They allege that the evidence they offer is new, was not put forward in the prior motions, or was not sufficiently highlighted in the prior motions.

III. DISCUSSION.

(A) Summary Judgment on the Issue of Materiality:

The Court's prior rulings intensely focused on the issue of materiality with respect to each of the statements in question. Although the present motion for summary judgment ostensibly raises the scienter aspect of the statements, defendants nevertheless again direct the Court's attention to the materiality question. Specifically, defendants raise questions about Statements ##5 and 10.

(i) Materiality of Statement #5 Revisited:

Statement #5 was made in a press release in late November 1982 and relates to the Twiggy disc drive. The statement is as follows:

> The Apple 871 Disk Drive [Twiggy] is the first high-density, double-sided disk drive mechanism to be built specifically for personal computer applications. It represents three years of research and develop-

ment and has undergone extensive testing and design verification during the past year.

The full text of the press release in which Statement #5 appeared was among the thousands of pages of documents submitted in connection with the prior summary judgment motion. On the basis of the parts of the press release that were put into issue before the Court, it appeared that Apple was representing that the Twiggy was a finished product. Indeed, the basis of the Court's denial of summary judgment on this statement vis-a-vis materiality was that "[t]he reasonable investor would infer from this that Twiggy was a product that was ready to perform." *Order* at 20.

After reviewing again the entire press release and receiving argument from the parties directed to that specific issue, the Court finds that it must amend the earlier decision with respect to the materiality of Statement #5. The reason is simple. At the end of the press release, badly reproduced, is the following section:

> *Price and Availability*
>
> Unifile and Duofile will be available in Spring 1983 from all authorized Apple dealers in the United States, Canada, and Europe. Unifile will retail for under $1,000 and Duofile will sell for less than $1,700.

Defendants never made reference to this section of the press release during the motion for summary judgment. Of course, they could not anticipate everything, however, and the Court should have paid closer attention to the full text of the press release instead of relying on the segments argued by the parties. The above quote is an explicit announcement that Twiggy only would be available (in the worst case) six months hence. Furthermore, Twiggy was indeed shipped in the Spring of 1983 as promised. Granted, Twiggy did not do all that had been

anticipated, but that is not the issue. The issue as framed in Statement #5 is one of timing. Quite simply, having stated that the product would not be available for another six months, defendants did not project the misleading idea that Twiggy was ready to perform at the time the statement was made. Accordingly, the statement was not materially misleading and not actionable.

On the basis of this analysis, there is no need to reach the issue of scienter. However, even if scienter is reached there may be no factual issue remaining. If the misleading aspect of the statement is that it gave the impression that Twiggy was ready to perform, and if defendants told the public that Twiggy would not be ready to perform until the Spring of 1983, then defendants could not have been reckless for they made precisely the type of disclosure about timing that one would require to avoid misleading the public. Regardless of the issue of scienter, however, the statement was not misleading and therefore not material.

(ii) Materiality Revisited Vis-a-Vis Statement #10:

A full discussion of Statement #10 is found in the Order at pp. 27-29. The text of the statement appeared in a *Wall Street Journal* article on April 13, 1983. The words are those of Apple marketing manager Barry Smith and they are interspersed at various parts of the article:

> [T]he Company has increased by 50% its estimate of how many machines it should make by the end of the 1984 first half.
>
> What we're finding is the reception of Lisa has been very strong.
>
> We find people willing to put down $10,000 without blinking an eye.

> [M]ore companies are willing to commit themselves to larger orders than Apple had expected. They're talking larger numbers for their first order, and a quicker reorder.

The materially misleading aspect of these representations is that the final two sentences give the impression that the pre-shipment orders for Lisa were *binding* orders, when in fact the orders were revocable without penalty any time prior to the shipment of the computer. In the Order, the Court indicated that "[i]t is conceivable that investors may have been aware that the commitments referred to in Statement #10 were non-binding, but defendants have not made such an assertion." *Order* at 29. If investors were aware that the orders were non-binding, then they would not have been misled, but without that information before it, the Court had to interpret the facts in the light most favorable to the non-movants and deny summary judgment on the issue of materiality.

Apple has now come forward with new evidence to establish that it was a generally known fact in the industry that orders for computers are "soft" (i.e., not binding) as a matter of course. The evidence Apple offers in support of this position are four declarations from industry experts.

The first expert, Stewart Alsop, states that he can recall reading the *Wall Street Journal* article in which Statement #10 appeared. Alsop states that his understanding at the time and at the present is that the Lisa orders to which Mr. Smith referred were not firm. Indeed, Alsop states that "in 1983, prior to shipment virtually all orders in the computer industry were cancellable at will by the buyer." According to Alsop, Mr. Smith used the term "order" in the typical manner for the industry referring to non-binding commitments to purchase computer products.

The second expert, Gregory Kelsey, essentially repeats the declaration of Alsop. The third expert, John Michael Murphy, also states that he and the industry understood that Apple's backlog was soft. The same is true of the fourth expert, Ulric Weil. Each of these experts is indeed an expert, an individual who is familiar with the market and who actually followed Apple stock during the period in question. At least two of these experts specialized in Apple stock and wrote reports and newsletters to investors on Apple's activities, as well as the activities and prospects of numerous other high technology computer firms.

In addition to these declarations, Apple has supplied an investors report prepared by a partnership entitled "Montgomery Securities" on June 22, 1983. In two parts of the sixty plus page report to investors, the authors explicitly state that the backlog for Lisa is "soft" and that all Apple orders are "subject to initial shipment evaluation and potential cancellation." This evidence further supports the declarations of the experts because it shows that investors were told that Lisa orders were "soft." In other words, following the fraud on the market theory, the price of the stock would have reflected the fact that the orders were "not firm." On this basis, disclosure by Apple, and Mr. Smith in particular, of the fact that the orders for Lisa were "soft" would not have altered the total mix of information already available on the market. A disclosure by Smith that the orders were cancellable at will prior to shipment would only have reinforced information already known (as declared by the experts) and available (as demonstrated by the Montgomery Securities' newsletter) on the market.

In terms of the summary judgment balance, the evidence offered by Apple is sufficient to meet its burden of production as the moving party to show that there is no triable issue of material fact. Under *Celotex v. Catrett*, 477

U.S. 317, 106 S.Ct. 2548, 2553-54, 91 L.Ed.2d 265 (1986), the burden is now on plaintiffs to come forward with evidentiary material raising an issue of fact about which a rational jury could differ.

Although plaintiffs do seem to recognize that despite Apple's description of this motion as being predicated on lack of scienter, the real issue (at least vis-a-vis Statements ##5 and 10) is materiality. Yet they offer little evidence to counter Apple's motion, instead stating that everything they have written before is incorporated by reference. The sole evidence they point to in refuting defendants' experts is a statement made in a May 1983 newsletter prepared by Gregory Kelsey (one of Apple's experts) which uses the words "buying" and "ordering" interchangeably. This is slim evidence. At best, it suggests some ambiguity, but it does not raise a triable issue of fact in the face of Apple's presentation. More likely, it reflects a technical inaccuracy by the newsletter, or it may mean exactly what it says, i.e., that some people are actually buying cautiously at first before they order in large quantities later on.

To sum up, defendants have come forward with a strong evidentiary showing as to the custom in the industry and have given a specific, explicit example of the manner in which the industry was aware of the potential ephemerality of the Lisa orders. On the other hand, plaintiffs have not come forward to take up their burden of production to demonstrate a triable issue of material fact. Under the recent Supreme Court cases, especially *Celotex* and *Anderson v. Liberty Lobby,* 477 U.S. 242, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986), summary judgment is now appropriate on the issue of materiality of Statement #10.

(B) Summary Judgment With Respect to Scienter:

The Order contained a lengthy discussion of scienter. That part of the Order discussing the legal standards

with regard to scienter, specifically pp. 40-42, is incorporated herein by reference. Applying those standards, the Court now will examine Statement ##10 and 15.

(i) *Scienter and Statement #10:*

As with Statement #5, the issue of scienter need not be reached if Statement #10 is not materially misleading. However, based on evidence presented in this motion the Court concludes that dismissal of Statement #10 also is appropriate due to lack of a showing of scienter.

Barry Smith was the individual who uttered Statement #10. He did so during the course of an interview; thus it was not a preplanned response which others at Apple directly participated in formulating. Any scienter connected with the statement could be attribued to Apple, but only through the person of Smith. Hence, assuming materiality for the sake of argument, the question is whether plaintiffs have made some showing that Smith intentionally or recklessly misled investors.

To begin with, Apple has offered the declaration of Mr. Smith. Smith states that he did not intend to imply that the orders for Lisa were firm orders. His intent was to emphasize that despite the $10,000 pricetag (which many analysts predicted would be Lisa's biggest stumbling block), many people were willing to file orders for the new computer. This is a plausible explanation and makes sense in the context of the *Wall Street Journal* article which focused heavily on the high price of Lisa (one can assume that issue of price was raised in the interview with Smith as well).

In connection with Smith's declaration, Apple makes the following argument. If Smith did not intentionally seek to mislead investors and did not knowingly do so (no evidence has been offered to prove the contrary), then the only way that plaintiffs can show scienter is by showing that the statement was made with reckless disregard for

its misleading character. In other words, defendants "had reasonable grounds to believe material facts existed that were misstated or omitted, but nonetheless failed to obtain and disclose such facts although they could have done so without extraordinary effort." *Burgess v. Premier Corp.*, 727 F.2d 826, 832 (9th Cir. 1984) (citations omitted).

Plaintiffs have introduced no evidence in this motion to show that Smith had reasonable grounds to believe that his statement about the quality of the orders was misleading. If the standard in the industry was that orders was cancellable at will prior to shipment, Smith would have no reasonable basis to be concerned about misleading investors. Plaintiffs have offered no response to the declarations of the market analysts who state that the industry practice was "soft." Plaintiffs have not offered the declaration of a single individual who allegedly was misled by Smith's statement. Nor have plaintiffs offered any counter-declarations suggesting that the understanding in the industry was anything other than that orders for Lisa were "soft" as with other computer products.

Under Rule 56 of the Federal Rules of Civil Procedure and recent Supreme Court opinions, it is not enough for plaintiffs to continue to rely upon the fact that Apple officials sold come of their stock during the class period. In fact, Mr. Smith is not a defendant in this action, nor is there any allegation that he owned and sold Apple stock during the class period. Thus, there is nothing to support plaintiffs' allegations of scienter. Accordingly, the Court concludes that not only was Statement #10 not material, but also plaintiffs have not shouldered their burden of making a prima facie case that Statement #10 was made with the scienter necessary to make it actionable under the federal securities laws. Accordingly, dismissal is proper on both grounds.

(ii) Scienter Vis-A-Vis Statement #15:

Statement #15 has proven to be somewhat elusive. The discussion of the statement in the Order is found at pp. 32-35. The statement was reconsidered in the Reconsideration Order at pp. 5-6. The statement is a five sentence blurb which appeared in a Reuters news service financial report in June of 1983. Apple spokesman Stanley DeVaughn allegedly stated:

> Apple began volume shipments June One [1983] of its new $10,000 Lisa Computer. "The product has been well-received and shipments are running ahead of expectations."

Originally, the Court found that the statement was not material because plaintiffs had not shown that it was a misstatement to suggest that expectations had been exceeded. On reconsideration, the Court took closer note of the first sentence of the blurb and concluded that in fact it was inaccurate because volume shipment did not begin until later in the month of June. Because of this inaccuracy, the statement was misleading.

Now, for the first time, Apple has submitted the declaration of Stanley DeVaughn, who at the time of his utterance of part of Statement #15 was Apple's manager of investor and press relations. Mr. DeVaughn does not appear to recall having had an interview with a Reuters reporter. Nor does he recall having made either of the statements attributed to him. If he did make the statements, DeVaughn states that they were an honest mistake not intended to mislead investors. Indeed, he points out that it was an objectively verifiable fact whether shipments of Lisa began in volume of June 1, 1983, and he would have no incentive to lie about such a fact.

DeVaughn states that he is able to identify the clipping which forms Statement #15 as having been sent to Apple by its press clipping service. Apple did not subscribe to the Reuters financial service. Documents received by

means of the press clipping service were received approximately six weeks after their publication. Given a publication date of June 13, 1983, Apple would not have received its copy of the clipping until late July or early August 1983, well after Apple in fact had initiated volume shipments of Lisa. This is significant in terms of materiality because by the time DeVaughn and Apple learned of the statement, it would have been too late to alter the total mix of information on the market by making a correctional statement to the public. Nevertheless, despite the absence of any continuing duty to correct, Apple officials still must face the fact that their spokesman issued a statement that was flatly wrong — a statement that investors may have relied upon.

As in the case of Statement #10, only one individual can be directly charged with scienter with respect to State #15. Like Barry Smith in his utterance of Statement #10, Stanley DeVaughn apparently made Statement #15 in the context of an interview. As such, the scienter behind the statement cannot be attributed directly to any of the defendants. If there was scienter, it had to be in the mind of DeVaughn which then could be attributed to the corporation and its executives through the controlling person doctrine. Indeed, all defendants have declared that they did not know of the existence of Statement #15 until this litigation arose.

Like Barry Smith, Stanley DeVaughn is not a defendant in this litigation. More importantly, as in the case of Mr. Smith, plaintiffs have made no showing of knowing or intentional conduct by DeVaughn. Mr. DeVaughn is not accused of selling any Apple stock during the class period, nor have plaintiffs demonstrated that DeVaughn had any particular knowledge or state of mind at the time of the interview. In the face of DeVaughn's declaration and in the absence of any evidence showing knowledge or intent to deceive, the burden is on plaintiffs' to show some

facts demonstrating that DeVaughn acted in bad faith. Plaintiffs have not done so.

The only way that the statement presents a triable issue is if DeVaughn acted recklessly in disclosing information to the public that was factually inaccurate. Under Ninth Circuit standards, Apple could be liable for DeVaughn's statement if DeVaughn had a reasonable basis to know that he was uttering a misstatement — regardless of DeVaughn's mental state. One could argue that DeVaughn should have known that his June 1 shipment date was incorrect. After all, he was a spokesman for Apple. Plaintiffs do not even argue this, they have nothing to say about the scienter argument.

The Ninth Circuit has said that recklessness is closer to "a lesser form of intent" than "merely a greater degree of ordinary negligence." *Vucinich v. Paine, Webber, Jackson & Curtis, Inc.*, 739 F.2d 1434, 1435 (9th Cir.1984), *quoting Pegasus Fund, Inc. v. Laraneta,* 617 F.2d 1335, 1341 (9th Cir.1980). Plaintiffs have presented no evidence whatsoever going to show anything beyond mere negligence on the part of DeVaughn. As the Ninth Circuit stated in *Vucinich,* "[a] plaintiff . . . must offer more than conclusory allegations, and if the defendant presents affidavits or other evidence establishing a lack of scienter, the plaintiff must come forward with some affirmative showing." 739 F.2d at 1436. This is precisely the situation here. Apple has offered DeVaughn's declaration contending good faith and lack of scienter. Plaintiffs have not responded in any fashion with an affirmative showing raising a triable factual issue. Therefore, summary judgment is proper as against Statement #15.

(C) Plaintiffs' Motion to Amend the Complaint:

On the basis of the above reasoning and conclusions, it is unnecessary to reach plaintiffs' motion to amend the complaint. With the dismissal of all of the statements, the federal claim is extinguished. Thus, there is no basis to

exercise pendent jurisdiction over the proposed state law claims. The parties report that plaintiffs continue to have two related actions on file in state court which parallel this litigation. Plaintiffs may pursue their state law claims in that forum, if appropriate.

IV. CONCLUSION:

The time has come to bring this litigation to a close. All that remains of plaintiffs' case are Statements ##5, 10, and 15. As described above, Statement #5 is not materially misleading. Statement #10 is both not materially misleading and has not been shown to have been made with the necessary scienter. Finally, plaintiffs have made no showing of scienter with respect to Statement #15. Having dismissed these claims, federal jurisdiction no longer exists; hence, the motion to amend the complaint need not be reached.

Good cause appearing therefor, defendants' motion for summary judgment is hereby granted. Plaintiffs' motion to amend the complaint is hereby denied.

IT IS SO ORDERED.

APPENDIX
E

CA No. 88-1617

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

In re: APPLE COMPUTER SECURITIES LITIGATION.

WILLIAM H. SCHNIEDER; CHARLES COHN; JEANNE COHN; ALBERT J. WHELEN, JR.; and ESTELLE B. ELLIS; Individuals, On Behalf of Themselves and All Others Similarly Situated,
Plaintiffs-Appellants,

vs.

JOHN VENNARD; DELBERT W. YOCAM; MICHAEL MULLER; WILFRID D. HOUDE; JOHN D. COUCH; GENE P. CARTER; KENNETH R. ZERBE; STEVEN P. JOBS; A.C. MARKKULA, JR.; JOHN SCULLEY; Individuals; and APPLE COMPUTER INCORPORATED, a California corporation,
Defendants-Appellees.

DC No. Cv-84-20148(A)-RPA
Cv-84-20148
Cv-84-20149
Cv-84-20158
(Northern California)

ORDER

Filed: January 18, 1990

Before: FARRIS, BOOCHEVER, and HALL, Circuit Judges.

The panel as constituted in the above case has voted to deny the petition for rehearing. Judge Farris and Hall have voted to reject the suggestion for a rehearing en banc and Judge Boochever recommends rejection.

The full court has been advised of the suggestion for an en banc hearing, and no judge of the court has requested a vote on it. Fed. R. App. P. 35(b).

The petition for rehearing is denied and the suggestion for a rehearing en banc is rejected.

APPENDIX

F

DEFENDANTS' COURSE OF MISREPRESENTATION[1]

"Statement No. 1":

Apple possesses unequalled strength, experience and expertise in the development, manufacture, marketing and support of personal computer systems. It is a form of equity accumulated during six years devoted exclusively to personal computing. Our ability to concentrate our resources on a single business has solidified our leadership and will sustain our market position in this important growth industry.

* * *

Several major products resulting from this effort will be announced in calendar 1983 . . . . A significant breakthrough in personal office systems will be among these introductions, aimed at professionals, managers and administrators within medium- to large-sized corporations. (Apple 1982 Annual Report to Shareholders, November 12, 1982, ER 7:664.)

"Statement No. 2":

"From all that I've seen so far, success should continue." (Apple 1982 Annual Report to Shareholders, November 12, 1982, quoting Apple Director Arthur Rock, ER 7:665a.)

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[1]The district court, and Court of Appeals broke the misleading reports and releases it examined into 16 statements, and numbered them 1 through 16. Although it is erroneous to approach each statement in isolation, because the case charges a continuous pattern of misstatements regarding Lisa throughout the Class Period, each building on the prior statements, for ease of citation, reference is made to the courts' numbers.

"Statement No. 3":

Apple refined its planning process in 1982, adopting a methodology consistent with company-wide operations. The process is based on a quarterly update program, during which changes from previous plan expectations can be communicated and acted upon as needed. (Apple 1982 Annual Report to Shareholders, November 12, 1982, ER 7:665).

"Statement No. 4":

Two high-density floppy disk products which provide new mass storage options for the Apple III personal computer were introduced today by Apple Computer, Inc. The Apple drives ensure greater integrity of data than other high-density drives by way of a unique, double-sided mechanism designed and manufactured by Apple. (November 29, 1982 press release, ER 7:748.)

"Statement No. 5":

The Apple 871 Disk Drive [Twiggy] is the first high-density, double-sided disk drive mechanism to be built specifically for personal computer applications. It represents three years of research and development and has undergone extensive testing and design verification during the past year. (November 29, 1982 press release, ER 7:750.)

"Statement No. 6":

Lisa incorporates the latest software and hardware technology. . .

* * *

Using LisaTerminal, a telecommunication software package being developed by Apple, Lisa functions as . . . an IBM-compatible terminal. When linked to Apple-Net, Apple's newly announced local area network, Lisa makes it possible for users to share peripherals and exchange

information and files (January 19, 1983 press release, entitled "Apple Introduces Lisa, A Revolutionary Personal Computer for the Office," ER 7:510, 515.)

"Statement No. 7":

"I don't think we will have any trouble selling all of the Lisas we can build." ("Apple Takes On Its Biggest Test Yet," *Business Week*, January 31, 1983, quoting Apple founder and CEO Steven P. Jobs, ER 5:152.)

"Statement No. 8":

"Lisa is going to be phenomenally successful in the first year out of the chute." ("Some Warm Up To Apple's Lisa, But Eventual Success Is Uncertain," *Wall Street Journal*, April 14, 1983, quoting Apple founder and CEO Steven P. Jobs, ER 7:411.)

"Statement No. 9":

"This division [that developed Lisa] is going to make Apple's growth before this look small." ("Some Warm Up To Apple's Lisa, But Eventual Success Is Uncertain," *Wall Street Journal,* April 14, 1983, quoting John D. Couch of Apple's Lisa Division, ER 7:411.)

"Statement No. 10":

[T]he company has increased by 50% its estimate of how many machines it should make by the end of the 1984 first half . . . . "What we're finding is the reception of Lisa has just been very strong . . . . We find people willing to put down $10,000 without blinking an eye . . . ." [M]ore companies are willing to commit themselves to larger orders than Apple had expected. "They're talking larger numbers for their first order, and a quicker reorder" . . . . ("Some Warm Up To Apple's Lisa, But Eventual Success Is Uncertain," *Wall Street Journal*, April 14, 1983, quoting Apple Marketing Manager Barry Smith, ER 7:411.)

"Statement No. 11":

We are extremely pleased with the market acceptance and orders to date for our Lisa personal office system. (April 28, 1983 Apple Second Quarter Report to Shareholders, signed by Steven P. Jobs, Chairman of the Board and A.C. Markkula, Jr., Vice Chairman of the Board, ER 7:414.)

"Statement No. 12":

The acceptance of Lisa among accounts has been very strong. I would say, however, that there has been one small surprise . . . and that is the interest by private individuals at the dealer level in Lisa. The demand in that channel has exceeded our earlier expectations. (May 6, 1983 Statement to Stock Market Analysts by Floyd Kvamme, Apple Vice President of Marketing and Sales, ER 7:433.)

"Statement No. 13":

"The interest by individuals at the dealer level has surprised us . . . . Major accounts are going about as we had expected," but orders are "higher than we thought from dealers . . . ." ("Lisa Backlog, Forecast For Rest of '83," *ISO World*, May 16, 1983, quoting Floyd Kvamme, Apple Vice-President of Marketing and Sales, ER 7:437.)

"Statement No. 14":

Hoar says the company is quite pleased with the level of orders placed for the Lisa which he says are double what had been anticipated at the release stage. ("Apples Old And New Have Good Fortune," *The Province*, June 5, 1983, quoting Apple Vice President of Communications, Fred Hoar, ER 7:438.)

"Statement No. 15":

Apple began volume shipments June 1 [1983] of its new $10,000 Lisa Computer. "The product has been well re-

ceived and shipments are running ahead of expectations," he said (*Reuter Financial Report*, June 13, 1983, quoting Apple Manager of Investor and Press Relations, Stanley DeVaughn, ER 7:711.)

"Statement No. 16":

Customer shipments of the Lisa systems began on schedule and we remain pleased with its market acceptance, order rate and dealer enthusiasm. Lisa is clearly being recognized as an important force in the office market. (July 27, 1983 Apple Third Quarter Report to Shareholders, signed by John Sculley, President and Chief Executive Officer, and Steven P. Jobs, Chairman of the Board, ER 7:441.)

PROOF OF SERVICE BY MAIL

STATE OF CALIFORNIA
COUNTY OF LOS ANGELES } ss.:

I am a citizen of the United States and a resident of or employed in the City of Los Angeles, County of Los Angeles; I am over the age of 18 years and not a party to the within action; my business address is 1706 Maple Avenue, Los Angeles, California 90015.

On April 18, 1989, I served the within Petition for Writ of Certiorari in re: "William H. Schnieder v. Apple Computer" in the United States Supreme Court, October Term 1989 No ....., on all parties interested in said action, by placing three true copies thereof enclosed in a sealed envelope, with first-class postage thereon fully prepaid, in the United States Post Office mail box at Los Angeles, California, addressed as follows:

M. Laurence Popofsky
Douglas M. Schwab
Heller, Ehrman, White & McAuliffe
333 Bush Street
San Francisco, California 94104
(415) 772-6000

Counsel for Respondents
Apple Computer, Inc., Gene P. Carter,
John D. Couch, Wilfrid J. Houde, Steven P. Jobs,
A.C. Markkula, Jr., Michael Muller, John Vennard,
John Sculley, Delbert W. Yocam, and
Kenneth R. Zerbe.

All parties required to be served have been served.

I declare under penalty of perjury, that the foregoing is true and correct.

Executed on April 18, 1990, at Los Angeles, California

J. Gordon Hooper

J. GORDON HOOPER